

/ POLICY PAPER



LESS REGULATION, MORE REPUTATION!

CASE STUDY: THE SHARING ECONOMY IN TRANSPORTATION
AND ACCOMMODATION.

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AUTHORS:



RÓBERT CHOVANCULIAK

Róbert Chovanculiak has been Economic Analyst at the Institute of Economic and Social Studies (INESS) since 2015. He is also currently a PhD student in the Department of Public Economics and Regional Development at the Faculty of Economics of the Matej Bel University, Slovakia. He worked as Analyst for the Slovak Business Agency prior to joining INESS. His field of professional interest is public finance, economic policy, new Internet technologies, and education.



ALES ROD

Ales Rod is Research Director at the Centre for Economic and Market Analyses (CETA). He earned his PhD (Economic Theories) at the University of Economics in Prague, Czech Republic, where he teaches various courses related to the field of Economics. His research deals with the principles and the effects of regulation, fiscal policy and public finances; he analyses shadow economy activities, banking and economics of luxury.



DESI SLAVA NIKOLOVA

Desislava Nikolova is Chief Economist of the Institute for Market Economics. She holds a PhD in Economics from the University of National and World Economy and a post-graduate research diploma from the University of Oxford. Her professional interests and expertise lie in the fields of macroeconomics and financial analysis; monetary policy, currency crises, exchange rates, behavioural and experimental finance and econometric modelling.



DOMINYKAS ŠUMSKIS

Dominykas Šumskis is a Policy Analyst at the Lithuanian Free Market Institute. His area of expertise is competition policy, ICT, sharing economy and business regulations. Dominykas mostly works with policy advocacy campaigns and research in the aforementioned fields.

Executive Summary

The emergence of the sharing economy shook things up in many sectors and within their regulatory frameworks. The greatest upheavals are currently being experienced by the taxi and accommodation services, since these are the services where the sharing economy has managed to compete with traditional service providers by (re-)employing idle capital.

Nevertheless, this is just one part of the influence of the sharing economy. The two aforementioned sectors are also characterised by rather extensive public regulation. This regulation is supposed to help mitigate the problem of asymmetrical information between service providers and their customers, i.e. to protect customers from inappropriate behaviour on the part of providers.

This is the point where the sharing economy influences traditional sectors indirectly. The sharing economy demonstrates that existing public regulations are not the only alternative to mitigating the problem of asymmetrical information. Another alternative is private regulation provided by platforms of the sharing economy.

Hence, the first half of the study focuses on the economic comparison of systematic tendencies which can be expected by these two different approaches to regulations (public and private). These systematic tendencies are divided into three main parts:

In the first part, we compare the incentive structure faced by creators of public and private regulations. The study shows that private regulation of platforms is incentive-compatible. This means it is in the self-interest of creators of private regulation to come up with the general welfare-increasing regulations. The opposite is true about creators of public regulation who, in the pursuit of their

self-interests, can often be subjected to pressure from various interest groups and thus create a regulation that will reduce general welfare.

The second part is concerned with the possibilities of public and private regulation to generate the knowledge necessary to create sound regulations, i.e. regulations which will not be too strict and thus too costly for service providers or, on the other hand, too lenient and thus constitute a too dangerous environment for customers. It is shown that private regulation has the possibility of unique feedback and “competition discovery processes”, which help to generate the necessary knowledge for creating sound regulations. On the other hand, creators of public regulations, with their monopoly power to create regulations for the whole sector, lack the feedback and self-correcting mechanisms.

The third part focuses on the problem of the enforcement of regulations. Even if one assumes that public regulations somehow overcome the first two problems, it does not mean that they will function without any problems. Enforcement of regulations can involve costs (transaction costs) which negatively affect their operation in practice. Nevertheless, it seems that creators of private regulation have come up with many innovative solutions (online reputation mechanisms, big data analysis) and have managed to decrease transaction costs in a better way than public regulation.

The second half of the study deals with the empirical description of regulatory frameworks and their development after the emergence of the sharing economy in four European countries: Slovakia, Lithuania, the Czech Republic and Bulgaria. The conclusion comprises summaries of the recommendations which are derived from the previous theoretical and empirical parts.

1. Introduction

Regulation of the commercial business sphere by the government is a relatively hot topic these days. According to a new study by Coffey, McLaughlin and Peretto (2016), the current GDP of the U.S. would be 25% higher if federal regulation had not increased since the 1980s. So why does one need to regulate a voluntary contract between two fully responsible parties at all? If both sides voluntarily agree to a contract, by definition both sides expect to gain. Otherwise, such a contract would not be entered into.

Currently, supporters of regulation most often cite the argument of the economic concept of information asymmetry. This is a situation where one party to the contract has an information advantage over the other (Akerlof, 1970). In general, the provider of the product or service is the more informed party who actually knows more about what is being sold than the buyer. Subsequently, as a solution to this “market failure”, the government began to recommend regulation by public authorities that would bring about a balanced relationship between provider and buyer. Thus, the term “consumer protection” came to be connected with the support of regulation. This approach to regulation will be referred to as “public regulation.”

Examples of such information asymmetry also exist in the areas studied in this paper, including personal transport and accommodation. For example, some taxi drivers in San Francisco at the end of the 19th century were called “nighthawks”. The term was coined because, instead of taking their customers to the location they had requested, they would drive them out to some faraway, abandoned place where they would then demand extra money for not leaving them there. These taxi drivers misused their information advantage with regard to the customer. Public institutions at

the time reacted promptly and issued a generally valid public regulation which prohibited a person from working as a taxi driver without a special licence. A condition for obtaining the licence was that the driver had to prove to officials that he was “a law-abiding citizen of good moral character.” (Anderson, 2013).

This approach to regulation – a monopolistic authority creates generally valid rules for the entire sector – was often the only solution in the last century. And if there was potential space for opportunistic action by service providers, the public authorities would as a rule react by limiting access to the field through licensing requirements, and imposing standards and rules, which were subsequently forced upon the providers and monitored through various inspections. However, this approach to regulation – “public regulation” – had its costs and shortcomings as well. Analytically, one can divide them into three areas: badly set incentives, knowledge problems and high transaction costs. In Part 2 they will be examined more closely. In Part 3, how the same problems are managed in private regulation will be analysed. Part 4 will present empirical analyses of four countries (Slovakia, the Czech Republic, Bulgaria and Lithuania). In the conclusion – Part 5 – specific proposals for public policy-makers on how to react to the arrival of the sharing economy in individual countries will be presented.

2. Three shortcomings of public regulation

In the second half of the 20th century, economists began to warn that, if the market did not produce optimal results, it would not automatically mean that intervention by a monopolistic (State) authority would best solve the problem. They started pointing to what they called “the nirvana fallacy” (comparison of the perfect state to the imperfect function of the actual market) and, instead of simple recommendations for intervention, they guided research efforts towards comparisons of how various institutional arrangements worked (Demsetz, 1972). Based on this approach, they discovered several shortcomings in the monopolistic approach:

THE ISSUE OF INCENTIVE STRUCTURE IN PUBLIC REGULATION

The first problem that public regulation faces is how to set the structure of incentives and the motivation of those who create them. If one wants to better understand the origins of public regulation, one must first let go of the assumption of the public sector as a benevolent creator of rules and regulations. Thus, the same (realistic) assumption must be applied to those who create policy as to other economic actors – they act in their own interests. In other words, it is naïve to assume that public authorities automatically create regulation which is in the interest of the public as a whole, instead of regulation that benefits the narrow interests of certain groups (Buchanan, 1999).

Economists have come up with several explanations of how regulation does not help “protect consumers”, but instead actually helps bring political rents to selected companies. They explain the “capture of the regulator”, who is actually captured by companies that he was supposed to regulate in the first place (Stigler, 1971).

The main problem is that the right to regulate entire branches of industry is in the hands of *temporary administrators* (with a monopoly on the creation of regulation). These actors can transfer the costs of their decisions on to the masses (e.g. consumers) and, on the contrary, direct benefits in the form of profits (rents) into the hands of narrowly defined interest groups (e.g. established service providers) that reward them for it. Expecting something else from those who create public regulation thus means expecting them to contribute (with their work, time or careers) to the public good in the form of laws created for the public benefit. Nevertheless, as economists explain, the public good has a tendency to be under-produced (Samuelson, 1954). So the same

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tendency for “under-production” will exist with public benefit regulation.

Furthermore, Mancur Olson (1984) showed that it is the smaller organised groups of service providers which will be more capable of coordinating and lobbying the creators of public regulation than large, dissipated groups of consumers. Moreover, established service providers often have an information advantage, not only over customers, but also over regulators (i.e. they know their true costs better). They can thus influence regulators’ decisions, and in so doing, secure regulation that suits them better. There is also a frequent phenomenon known as the “revolving door”, where the same people move between employment as a regulator and employment with a regulated firm, thereby perpetuating the above-mentioned capture of the regulator.

In the first example cited in the introduction, where public regulation was supposed to be a tool against “nighthawks”, it is also possible to find elements of the “capture of the regulator”. Public regulation in San Francisco stipulated that for one registered vehicle, there could only be one licensed taxi driver. This efficiently protected against the entry of new competitors from other states, who were more effective in providing transportation (they charged lower prices). The reason for their effectiveness was above all the fact that several drivers used the same vehicle during the day and night. Independent drivers in San Francisco, who were attached to one vehicle and represented by the Carriage Drivers’ Protective Union, did not like this. This Union actively supported the above-mentioned public regulation prohibiting multiple drivers from using the same vehicle.

With regard to public regulation, there will always be a systematic tendency for the creation of regulation that will, rather than protect consumers, protect the monopoly position of several selected providers. The result of this is several types of ineffectiveness which economists have described: a “deadweight loss” (less mutually beneficial exchange will take place than would take place without regulation); “rent-seeking” (entrepreneurs spend resources on gaining political advantage and not on satisfying the needs of consumers); and “X-inefficiency” (there is no pressure of competition driving the effective management and

operation of firms and no pressure to innovate). In a broad study by Matthew Mitchell (2012), the author recorded numerous real-world examples where the regulator was captured by companies that were supposed to be regulated, leading to exactly this type of ineffectiveness.

A KNOWLEDGE PROBLEM WHEN SETTING PUBLIC REGULATION

If one was to assume that a regulator has the best intentions (i.e. one ignores the problem of a bad incentive structure), there remains the problem of identifying and creating the correct regulation (i.e. knowledge problem).

Regulation creates various costs and benefits for the individual parties to a contract. Even the same piece of regulation can mean more costs than benefits for one side and more benefits than costs for the other side. How is a public regulator to decide whether to approve such regulation? If a regulator accepts strict conditions governing licensing for entrance to a field (for example, every hotel room must have air conditioning), high costs are created for providers. However, at the same time benefits are provided to consumers, who thus receive higher quality service (the guest can be sure that the room will never be too hot). Thus public authorities face a knowledge problem when the costs of strict regulation are justified for providers, because they are more than compensated for by the benefits provided to consumers.

The principal challenge of a central public regulatory authority is to create rules and regulations that are sufficiently strict or lenient to generate more benefits than costs on the whole for all the actors involved. In other words, they result in the maximum total net gains.

However, when creating public regulation, the regulator does not generally possess the necessary knowledge of the specific time and place that is needed to evaluate individual costs and benefits correctly for various parties to the contract. A public authority with a monopoly on blanket regulation valid for the entire economy also has no feedback that could assist it in finding out *ex post* whether the regulation in question generates net benefits or losses. There also exists no competitive pressure,

which would help to expose such unsuccessful regulation.¹ What is more, market conditions are continually and rapidly changing, which alters the relative costs and benefits of regulation, and also presents a plethora of new methods for resolving the problem of asymmetric information and opportunistic behaviour. Nonetheless, a public authority is not flexible enough to react to these changes, since it cannot evaluate their relative advantages and does not have feedback available to it.

For example, within the realm of the taxi service in the Slovak Republic, it is prohibited to register as a taxi an automobile which is more than eight years old. This regulation obviously represents costs for the service provider, who is forced to buy a newer car than he might have done if the regulation did not exist. On the other hand, it provides certain benefits to the customer who, thanks to the regulation, can travel in newer automobiles. Nevertheless, the question is whether this regulation produces net benefits in reality. Customers might be more willing to travel in older cars and pay lower prices. But the public regulator has no way of knowing whether the arbitrary decision was a good one and has no feedback available to assist in overcoming this knowledge gap. And its public regulation is generally valid throughout the entire territory of the country, so there is no pressure of competition.

THE HIGH TRANSACTION COSTS OF PUBLIC REGULATION

If one assumed that public regulation was created by actors according to the well-being of society as a whole and that somehow they have managed to discover the correct types of regulation, it still does not guarantee the optimal functioning of public regulation. The reason for this is the high transaction cost which causes regulation, despite its correctness or quality, to function differently from what it should. Regulation is far from self-enforcing and requires an active approach, whether from the side of those monitoring it, the subjects of the regulation themselves, or their customers.

An example of this could be the provision of taxi services as researched by us. For example, the public regulator in the Slovak Republic established rules for the correct provision of taxi services. If these rules are violated, customers can turn to an inspector. The latter will then issue a fine to the taxi driver or even confiscate his or her licence. Under Law no. 56/2012 on road transportation, a taxi driver is obliged to let customers see the meter during the trip from beginning to end, and to take the shortest route possible, given the traffic situation. Another route can be taken only if the customer agrees to it or proposes it him- or herself.

Even if one assumes that these regulations are optimally set, there remains the problem that, from the customer's point of view, it is often difficult to recognise a violation. And if a customer can identify one, there are relatively high costs associated with pointing it out. The result is regulation that does not function optimally – it is not enforced. This is also the reason why taxi drivers in various cities often have a dubious reputation, despite the existence of regulation. In fact, taxi drivers know that the existing public regulation is often not enforced, and that they can abuse their position with regard to the consumer to their advantage, without real consequences.

Similarly, a central authority can issue the correct standards of quality and rules of service provision, but if it does not have sufficient control or resources, the regulation remains without real influence. For example, the Transportation Regulation Authority of the Slovak Republic (SR) has the right to levy a fine of 100–15 000 euros on taxi drivers who charge prices that do not correspond with their normal tariffs. And despite the existence of this public regulation, there are relatively frequent examples of drivers overcharging tourists fares far above the official taxi tariff.²

Thus, the result can be a situation where despite the *de jure* existence of the correct public regulation, the relationship between the service provider and the consumer will *de facto* be unregulated. And in this case, there will continue to be room for opportunistic behaviour.

¹ In other words, the creation of public regulation suffers from the same problems that central planners encountered when operating socialist economies without access to prices and the possibility of calculating profits and losses. See Mises (1920) and Hayek (1935).

² The problem is a slow and costly legal dispute resolution, which can also ultimately hinder the function of the regulation.

3. The sharing economy and private regulation

However, public regulation is not the only alternative. One does not face the choice between public regulation or no regulation at all. There is a third alternative – private regulation – which in recent times has been popularised above all by the sharing economy. The following sections examine what the sharing economy is and how it has helped to mitigate the three problems of public regulation mentioned above.



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THE SHARING ECONOMY IN BRIEF

An alternative to the centralised approach to regulation as described above has been introduced by an IT revolution in the form of Internet. At the turn of the millennium, the Internet was generally used as an “electronic newspaper”. That is, an average user mostly took information from Internet pages in a passive way. With the appearance of Web 2.0 applications, however, it became possible and easy to participate actively in creating content and coordinating a large quantity of people at low cost. Thus the first platforms enabling communication and online collaboration, the first social networks with virtual communities and mobile applications enabling interaction from practically any place in the world, began to appear. In addition to a revolution in blogging, social networks and crowdfunding, there was a revolution in the sphere of sharing. This brought with it (in addition to many other things) some interesting solutions to the problems of the information asymmetry described above. Specifically, this was in the area of private regulation through competition among decentralised platforms in the sharing economy.

Before sharing economy platforms emerged, numerous potentially advantageous exchanges existed, which were never implemented because of high transaction costs. It could easily happen that someone had a long unused drill at home, while at the same time someone in the next street needed one. What prevented the drill from getting from the hands of the first person into the hands of the second was that they simply did not know about each other. And if they did know, it would have been difficult for them to agree on a price; and if they did agree, they would have had to sign a contract; and if they had signed one, there would still be the problem of its enforcement and control. In other

words, what prevented advantageous exchange was the above-mentioned high transaction costs. And it is here, in the lowering of these costs, that the sharing economy platforms have begun to function – and to achieve a profit (Munger, 2015).

Above all, the last part – that of transaction costs for “enforcement and control” – is highly relevant for this study. This is exactly the point where the platforms have managed to replace and even surpass existing public regulation. In other words, in many traditional fields, the sharing economy brought with it an alternative to public regulation. An alternative in the form of a decentralised approach to the creation of private regulation. Subsequently, with the aid of various mechanisms and systems, it creates trust between the two parties to a contract and mitigates the problem of asymmetric information, simultaneously solving all three of the problems of public regulation described above.

In addition to a more intensive use of resources (through sharing, renting and facilitating services), the sharing economy has also enabled the identification and pointing out of existing ineffective public regulation and then replacing it with higher quality private regulation. How it has achieved this is the subject of the following sections.

THREE ADVANTAGES OF A DECENTRALISED APPROACH TO PRIVATE REGULATION

Aligned incentives in private regulation

The owners of platforms are the creators of private regulation. In contrast to politicians – the *temporary* administrators – who are responsible for creating public regulation, the makers of private regulation are the owners of the platform’s equity. Thus, they have an incentive to approve rules and regulations that will maximize the value of their platforms in the long term.

For this reason, the owners of platforms in pursuing their own interests have to take into account the interests of all of the platform’s participants, i.e. the service providers as well as the customers. The only way platform owners can make a profit is to create an environment (rules and regulations)



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that secures the maximum number of commercial transactions. So it is in the personal interest of private regulators to ensure that the platform is safe and that individual actors will be willing to sell, share, rent and provide services to the greatest extent possible.

Platform owners know that if individual actors feel secure, they will be willing to pay an increasing amount for services and enter into a larger number of contracts. This is how platforms generate income. And this is the reason why platforms in the sharing economy cannot be captured, as is the case in public regulation.

So income and wealth for a platform owner are thus directly dependent on how well the own private regulation can be set up. The incentives are aligned with the interests of the customers, just as, for example, with regard to Adam Smith’s well-known baker:

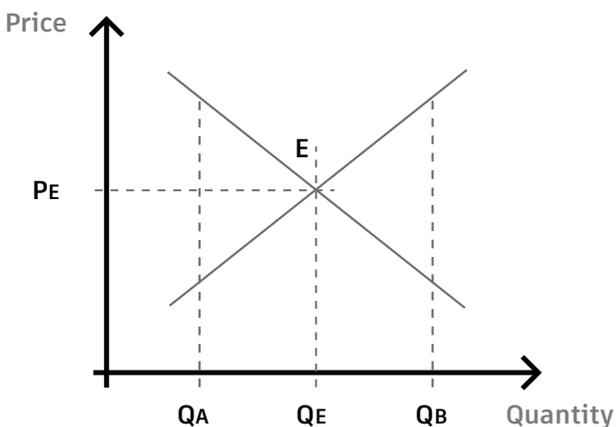
“It is not from the benevolence of the butcher, the brewer or the baker, that we expect our dinner, but from their regard to their own self-interest. We address ourselves not to their humanity, but to their self-love, and never talk to them of our own necessities, but of their advantages.”

One does not necessarily expect anything different from the creators of private regulation, except that they will serve their own interests. In the case of public regulation, it is exactly the opposite. The establishment of regulations that uplift the well-being of society would require good intentions on the part of politicians and regulators.

COMPETITION AMONG PRIVATE REGULATION THAT GENERATES KNOWLEDGE

In contrast to the creator of public regulation, a platform owner who creates private regulation does not have the opportunity of imposing his ideas about the correct way to regulate (for example, in the area of personal transport) on all the other participants in the economy. Nevertheless, a platform owner possesses the opportunity of limiting access to his own platform – for those who do not fulfil the rules and regulations required by it. The owner can therefore regulate the conditions on his own platform. Thus, there emerges a space for competition among decentralised platforms in the creation of private regulation.

This competition helps to resolve the knowledge problem present when creating public regulation, which was described in the second section of this study. Correct regulation must, after all, possess several attributes simultaneously. The same piece of regulation can bring both utility to the customer and unjustifiably high costs to providers. In the process of competition, entrepreneurs will discover that extent of regulation where the marginal costs will equal the marginal benefits (Graph 1, point E). That is, regulation, which maximises the net benefits resulting from it. If, for example, one



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THE CREATORS OF PRIVATE REGULATION HAVE AT THEIR DISPOSAL FEEDBACK IN THE FORM OF PROFITS AND LOSSES.

adopted regulation which was too permissive (the left side of Graph 1, i.e. points QA to QE), there would be an opportunity for advantage through tightening the platform’s safety regulations. This is because customers would be willing to pay more for higher security than the actual costs linked with the regulation itself – in economic terms, $MU > MC$. In the opposite case (the right side of Graph 1, points QE to QB), there would be a profit opportunity in abolishing regulations that are too strict (this is the reason why the private sector has the tendency to avoid excessive and unnecessary bureaucracy, in contrast to the public sector). The optimal level of regulation is found at the point where the marginal costs equal the marginal benefits of the added strictness of regulation.

However, in principle, private regulators by themselves do not have any better access to knowledge (than that needed to create the correct regulation) than the public regulator. They do, however, have access to feedback, and at the same time, are part of the process of market competition. With the aid of trial and error, market competition enables them to generate the required knowledge important for avoiding bad business decisions, while imitating and developing successful ones.

This characteristic of market competition was best described by the economist Friedrich von Hayek (1968) who expanded the static understanding of competition to include its dynamic nature in the form of entrepreneur discovery. Later, he also applied this approach, in addition to relationships

within the market, to the creation and emergence of law as an alternative to legislation (Hayek, 1973). Later, he showed how this same process of dynamic discovery can also function in the monetary sphere where, according to him, competition between currencies should help to discover the correct form of money (Hayek, 1976).

Today one can observe this process of dynamic discovery, thanks to the sharing economy and its platforms, as well as in the regulation.³ Private regulation thus enables parallel functioning of several regulatory frameworks, among which is competition. Moreover, the creators of private regulation have at their disposal feedback in the form of profits and losses, or the waxing and waning of customers and service providers. This process helps them to select the correct types of regulations – bringing in those that result in net gains and getting rid of those that do not work.

For example, Uber established many conditions that interested service providers must adhere to on its platform. In some areas, these requirements are looser than those imposed by public regulation (vehicle inspections, psychological testing, knowledge testing), while in others they are stricter (e.g. driver screening and insurance levels) (Feeney, 2015). For example, Uber also requires that cars are not older than 10 years, that drivers have no criminal record, (unpaid alimony is an exception) and have a minimum of three years of driving experience. Uber requires that one enters their payment card information to join the platform, and also has completely eliminated cash transactions (in so doing, it has significantly increased the safety of both drivers and customers). It also regulates its rates and a pairing mechanism – customers may not choose a driver themselves, but can refuse one that is assigned to them; similarly, the driver sees the demand for his or her services, but cannot see the destination for a trip. Moreover, Uber provides information on how demand for transport is evolving or will

evolve. And Uber insures its drivers and third parties against risk of up to one million euros.⁴

All these rules are merely attempts within the discovery process and other platforms can offer other solutions. For example, Lyft, the competing platform, enables customers to tip drivers – which Uber prohibits. Lyft also uses a different algorithm for matching and generating prices, surveys its drivers in more depth via interviews, requires drivers to mark their cars with a “fake pink moustache”, offers a more personal approach with a greater representation of women and has an Emergency Call Centre operating 24/7.

A similar discovery process for the correct regulations also exists on accommodation platforms. For example, Airbnb worked for a long time on designing the parameters in its disclosure system. Based on its own analyses, Airbnb came to the conclusion that, if on first contact, people revealed too little or too much about themselves, their willingness to accept a guest decreased. The optimum was somewhere in the middle. For this reason, they designed a special acquaintance form for first contact where the guest has to answer three questions for the host: “tell us something about yourself; what brings you to the city and who is coming with you; and what did you like about our accommodation?” The space for the answers is set out precisely, so that answers are neither too short nor too long. The result is a higher level of trust between individuals on the platform.

³ Similar competition in the field of rules, regulations and security creation exists, for example, among proprietary communities, condominiums, hotels, shopping malls, amusement parks, etc. (Beito, Gordon, Tabarrok, 2009). The first rules and private regulation of stock exchanges emerged in a similar way in 17th-century Holland and later in England (Stringham, 2002 and 2003).

⁴ This insurance becomes active only from the moment the Uber application is opened and the customer gets into the car. The moment the application is closed, the vehicle is covered only by normal compulsory insurance. A problematic situation emerged when the application was turned on, but the customer was not in the car. In this case, Uber provided only supplemental insurance known as “contingent liability coverage”. In time, a type of insurance covering exactly this kind of situation came on to the market in the U.S. This insurance product is not as inexpensive as the classic non-commercial insurance, nor is it as expensive as the commercial insurance that taxi drivers use.

RADICAL DECREASE IN TRANSACTION COSTS OF PRIVATE REGULATION

In the previous section, it was shown how even the correct public regulation approved by benevolent regulators can be ineffective, if its enforcement is associated with high transaction costs. That is, this sort of public regulation works only *de jure* and not *de facto*. As platform owners, private regulators cannot afford this. Within the process of entrepreneurial discovery, they have brought various mechanisms to bear, which enable a radical decrease in transaction costs for enforcement of private regulation. Examples of these are, above all, reputation systems and big data analysis.

Reputation systems allow for mutual evaluation by the individual parties to a contract. Customers say how satisfied they were with the service, and providers indicate how satisfied they were with the customer. Such reputation systems immediately create two-sided pressure on the parties to behave well and to refrain from abusing their information advantage. 1) The parties to the contract are *ex ante* motivated only to look for and enter into contracts with another party that has a positive evaluation and, thus, has behaved according to expectations in the past. 2) Subsequently, during the contract, the parties are motivated to uphold the rules of the platform and to avoid opportunistic behaviour, since they will then receive *ex post* a poor evaluation.

Reputation systems thus improve cooperation, act as enforcement mechanisms, help signal trustworthiness and quality, lower risks, and motivate good behaviour while punishing bad. In other words, they assist in solving the problem of information asymmetry.

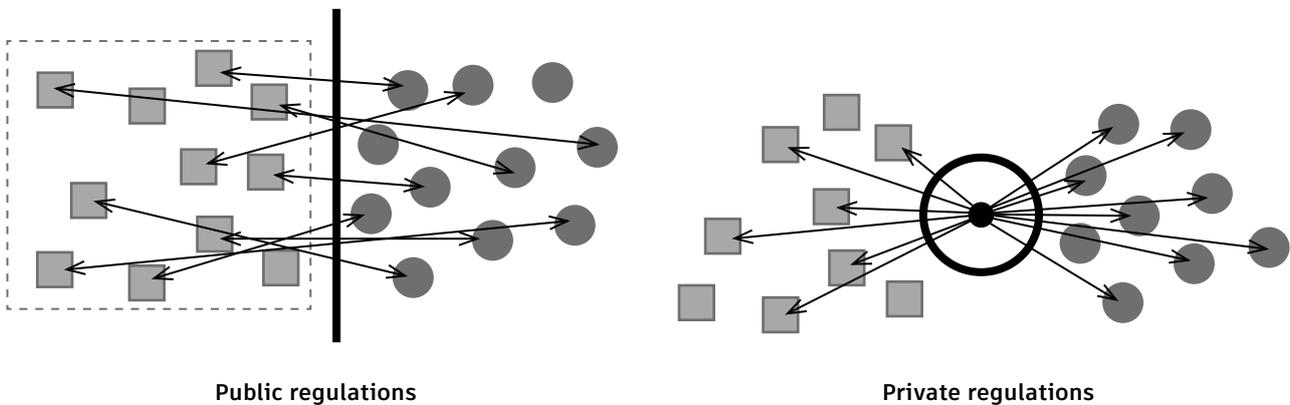
If a driver on the Lyft platform receives an evaluation of less than 4.6 stars out of 5, his account will be deactivated. Alternatively, if a customer gives a driver less than three stars, he or she will never again be paired with that driver. These mechanisms are also used effectively by a platform called Feastly, which links home cooks who are willing to prepare dinner at home, with potential customers who are willing to eat at someone else's house and pay for it. In this way, reputation systems help resolve even those situations where there is a high level of information asymmetry.

These systems replace anonymous interactions between random actors with interactions that happen in a centre (the platform). This platform records the history of these interactions and thus helps to eliminate anonymity and to create trust. On the left side of Figure 1 (see p. 13) are squares depicting drivers and, on the right, circles depicting customers. The arrows represent contracts between taxi drivers and their customers. Under classic public regulation, there is an effort to define correct service provision and then to enforce it (marked by the blue border lines). However, this method of enforcing regulation is very costly and often unreliable.⁵

The establishment of a contract between the provider and customer under public regulation is, however, formed on a random basis and remains to a large extent anonymous (random arrows). The customer does not know the taxi driver's history, and potential opportunistic behaviour does not affect his future reputation in any way. The taxi driver is motivated to externalise the costs of his bad behaviour on to other taxi drivers, thus damaging the reputation of all taxi drivers.

The exact opposite happens on the lower part of the figure, where there is a diagram showing how transportation of persons through the platform works (all arrows aiming at the big black circle). Here, the customer knows the driver's history and the latter cannot externalise costs to other drivers through bad behaviour. Instead, the costs remain internalised with him. This, of course, creates the pressure to behave well.

⁵ For example, for years, regulators in Las Vegas had a problem with taxi drivers who cheated tourists by driving them the long way from the airport in order to make more money. The local regulator had tried everything: from classic issuance of standards for taxi driver behaviour and police monitoring of the drivers' routes to large information tables showing the right route or creating a system where travellers could submit complaints. They even had a plan for requiring the installation of new surveillance equipment that would monitor whether a taxi driver was cheating customers. None of these were effective (Ross, 2014). This problem in Las Vegas was finally resolved by Uber with its private regulation and reputation systems. And only until the moment it was banned (a year later it was allowed again).

Fig. 1 Public vs. private regulation in personal transport

Another method used by platform owners to decrease information asymmetry is “big data” analysis. This sort of analysis uses computer algorithms to monitor millions of transactions and, based on the certain keys, block or mark those that are suspicious. The latter are then sent to a team of investigators for deeper analysis.

In all three problematic areas (incentives, knowledge and transaction costs), private regulation in the sharing economy brings with it the theoretical tendency as well as the empirical experience to outdo public regulation by public authorities. If one takes these tendencies and experience seriously, the sharing economy can represent not only a tool for realising mutually beneficial exchange that would not otherwise occur,⁶ but can also be a tool for the identification and overturn of old, dysfunctional and ineffective public regulation.

THE SHARING ECONOMY AS A LITMUS TEST

As was shown in the first part of this paper, the mere existence of public regulation in the legislation does not automatically mean that it is economically or socially justified or even beneficial. The opposite is true in several cases. Despite the fact that public regulation of the business environment normally presents itself as assistance to consumers, many public regulations are more a result of pressure from interest groups or excessively active and naïve politicians (regulators).

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REPUTATION SYSTEMS
THUS IMPROVE
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HELP SIGNAL
TRUSTWORTHINESS
AND QUALITY, LOWER
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GOOD BEHAVIOUR
WHILE PUNISHING
BAD.

⁶ A new study by Krueger and Cramer (2016) finds that Uber drivers can use their time much more effectively when they are driving. They spend 30-50% less time and drive 30-50% fewer kilometres with an empty vehicle than normal taxi drivers. So Uber not only outdoes the old regulation, but also enables more effective use of time and space.

In this case, it would be better from the consumer's point of view if the particular regulation were abolished or not formally enforced. Yet in practice it is not easy to recognise when the costs of public regulation are higher than its benefits and when it rather benefits a concentrated interest group than dissipated and disorganised consumers.

When resolving this problem, on the one hand one can try to rely on political processes and democratic mechanisms. Nonetheless, this takes a long time and in some cases one cannot even expect to see such changes. The problem is information asymmetry between voters and politicians on one side and between consumers and interest groups on the other. Voters simply do not have the motivation to inform themselves daily or to monitor politicians as to whether they are approving only regulations that increase public well-being. So politicians have wide room to manoeuvre when performing their legislative-regulatory roles. It is as difficult for people to evaluate whether, from the point of view of consumers, the regulated branch would function better or worse without public regulation. The consumer would have to undertake some complex thinking about how the world would appear without a specific piece of public regulation.

One is getting into a paradoxical situation here. As was illustrated in the introduction, information asymmetry is presented as one of the main arguments for bringing in regulation (the producer or service provider knows more than the customer) and, at the same time, one of the main reasons for the ineffectiveness of these public regulations (the voter and consumer cannot monitor politicians or identify ineffective regulation).

It is, however, the sharing economy with its private regulation that can help to break the thick political ice. The sharing economy disrupts old public regulation. And it does it in such a way as to test the net benefit resulting from it and simultaneously to mobilise people to political action. In this way, it solves two of the problems described above.

1) In the sharing economy, consumers, through their buying decisions, compare classic services

under public regulation with services based on new technology and private regulation. In this way, they test the relative effectiveness of public regulation vs new private regulation in the sharing economy. The sharing economy thus lets customers experience what a service which is not publicly regulated looks like – a service that solves the problem of information asymmetry through the private rules of a platform. If public regulation is truly justified, then its private alternative should collapse into a spiral of dysfunction due to customer dissatisfaction from information asymmetry (as the theory of usefulness of governmental regulation predicts).

2) The sharing economy therefore also enables the mobilisation of people and the creation of pressure on politicians whose room for manoeuvre is thus decreased. The latter then give in to the people's will. For this reason, it is a highly democratic way of changing regulation. A recent example of such a series of events took place in New York City, where Mayor Bill de Blasio attempted to limit the number of drivers allowed to drive for Uber. There was a large wave of protest against this by ordinary citizens, and de Blasio, who had officially received campaign contributions of \$500 000 from the taxi lobby, had to withdraw the proposal. Because of Uber's popularity and the pressure brought to bear by the public, New York has one fewer bad regulation (even if the old regulation is still in place). Mayor de Blasio had to give in to the voters.

An even fresher and more interesting example comes from the city of Sarasota, Florida where the city council was supposed to vote on the proposed regulation of Uber. The proposal was to impose all the existing regulation for classic taxi drivers on Uber as well. Uber reacted to this by threatening to leave the city. Once again, this made for an angry public, which had become used to Uber and considered it as something positive. Finally, not only was councilwoman Susan Chapman's proposal not accepted and Uber not regulated, but the existing regulation on classic taxi drivers was unanimously abolished.

EU INSTITUTIONS AND THE SHARING ECONOMY

At the beginning of 2016, the European Parliament commissioned a study, the main conclusion of which was that the sharing economy could potentially bring Europe added value of as much as 572 billion euros annually. This would occur mainly because of better utilisation of valuable resources and capacities. The study's conclusions are positive about the sharing economy, but warn of the possible risks represented by, above all, extreme reactions by governments in the form of regulation and limitation of functions of the sharing economy. Eventually, these reactions could shrink its added value.

Another EU institution addressing the sharing economy is the European Court of Justice. It is expected to decide whether Uber will be considered a transportation service or a technology firm. Based on this decision, Uber will be subject to various regulations and limitations under EU law. Quite recently, the European Commission (EC) has published guidance and policy recommendations. The relatively positive stance of the EC toward the sharing economy's benefits should be welcomed. The EC literally points out that the sharing economy offers marked benefits and represents new opportunities for the future.

The EC's call on governments to release the sharing economy from highly restrictive and often unjustified limitations should also be welcomed. And this is predominantly the case in situations where the effects and results of the sharing

economy have not been sufficiently researched, while at the same time there exist much less limiting approaches than "prohibit it completely".

The EC also points out to member states that they can use the sharing economy's arrival to re-evaluate the added value of existing public regulation. That is, above all, its frequent shortcomings, which were indicated above in this paper. At the same time, the EC underlines the function of "rating and reputational systems or other mechanisms" within the sharing economy, which can, according to the EC, "reduce risks for consumers stemming from information asymmetries". And thus, "this can contribute to higher quality services and potentially reduce the need for certain elements of regulation".

On the other hand, the EC refused to set a type of "maximum" regulation limits and often admits evaluating the appropriate level of regulation on a "case by case" basis. This approach raises concerns that too many countries or regions can claim their situation as unique and apply restrictive regulations. And the result will be exactly what this study and the EC fear and warn against.

Nevertheless, trying to create uniform regulation for the sharing economy on the EU level is not a solution either. The problem is that State public regulations that have to be changed as a result of the sharing economy are very diverse in different countries: taxes, labour codes, social policy, licensing, establishment of a business, etc.

4. Empirical analyses of regulation in four countries

SLOVAKIA

Regulation of taxi drivers in Slovakia

Every taxi driver who wants to provide an independent taxi service must obtain a trade licence to be self-employed. Obtaining the licence itself is relatively simple – it takes one to three days and costs about €10. However, the real cost increases due to mandatory contributions and taxes. During the first year, a self-employed person pays health insurance contributions only, but if his or her annual gross income exceeds the limit of €5148, social insurance contributions must be paid the following year. The minimal social insurance contribution is about €150 per month, and the minimal health insurance contribution is about €60 per month.

Providing a taxi service also requires a taxi licence. Firstly, a potential taxi driver must undergo a series of tests and examinations to verify his or her professional, health and psychological competence to drive a taxi. Later, a special examination of the taxi driver (written, oral) must be passed before a taxi licence is issued. In addition, the driver must have been in possession of a regular driving licence for at least 3 years and must be 21 years of age or older.

The fee for the exam is €50. The main problem is that these exams take place within a regulated district (Bratislava, in this case) only once every 3 months for 50 participants.

To pass the exam, it is recommended to attend a specialised seminar in which the applicant gets

to know about the exam topics. The seminar fee is about €65. When a potential taxi driver passes the exam, a request can be made for a taxi driver's card which costs €50.

Then the potential taxi driver must undergo psychological tests to provide proof of psychological skills mandatory for each taxi driver, which costs from €60 to €80, and also undergo health examinations. Financial resources of at least of €1000, by a certified statement of assets and liabilities, in addition to a copy of a clear criminal record statement must be demonstrated.

If a taxi driver has met all the personal requirements, the equipment requirements must be considered. A vehicle used as a taxi cannot be older than 8 years and a driver must provide proof of its ownership. A vehicle has to pass a technical inspection and emission test every year (€50). A vehicle must be marked with the trade name of the taxi company and the banner inscription 'TAXI' on the roof and on both front doors, in addition to the telephone number of the taxi service (€70). The taxi driver must install a transport schedule and taximeter in a visible place (€400) in the interior. A vehicle must be insured against liability for damage caused by the operation of road passenger transport, passengers, baggage and third parties (€120 annually).

After a taxi driver has met all these conditions, regulations and requirements, district authorities issue a licence for the taxi service. The total initial cost, apart from time cost, reaches an approximate amount of €950 (see Tables on p. 24–27).

The arrival of Uber in Slovakia

Uber came to Slovakia (to the capital city, Bratislava) quite late – in the middle of 2015. It began to provide its services of shared personal transportation without complying with the regulations described above. After a couple of months, some taxi drivers staged a mass protest against Uber, which resulted in more intensive communication between Uber and public institutions. Thereafter, Uber pledged to fulfil the mandatory requirements.

Since 2016, Uber has required its drivers to have a business licence for being self-employed. It has also committed to ensure that its drivers pass the test of professional skills. However, as stated above, these tests are available only four times a year for approx. 200 people per year. The local manager of Uber in Bratislava has estimated that if they wanted to meet this obligation with all of their drivers, it would take them several years. Therefore, drivers of Uber have gone on to offer services without taxi driver licences.

The situation is currently at the waiting stage and Uber continues to provide its services in spite of the fact that it does not comply with the official public regulations. The biggest problem is that Uber drivers, with the current obligation to have a business licence as self-employed persons, are motivated to drive only to a point when their annual gross revenues do not exceed €5148, as they do not want to pay the high minimum social contributions.

And this is perhaps one of the reasons why Uber remains a relatively small transportation phenomenon in Bratislava. In fact, approximately 3500 taxi drivers operate there, while Uber drivers account for only only approx. one-tenth of this number.

Regulations of accommodation services

If a person wishes to rent out property in Slovakia on a regular basis and provide basic services (water, gas, electricity, etc.), as well as additional services, such as linen change, breakfast, cleaning, etc., it is necessary to have a licence for being self-employed which presents additional costs – especially in later years of business if the amount of gross revenue exceeds €5148 annually (as described above).

If the owner wants to rent out a property, which has passed inspection for private use only, he must request a construction office for a change in the use of the construction. To do this, it is necessary to submit an application to the competent construction office (€30) with relevant documents (verdict of inspection, sketch of the building, list of ownership and copy of cadastral map), and subsequently, to perform a personal check of fire extinguishers and compliance with hygiene standards (€50). If everything is in order, the competent construction office will begin a re-inspection with its own personal control. The whole process can take from 30 to 60 days.

Thereafter, the host must be familiarised in detail with the Decree of the Ministry of Economy of the Slovak Republic No. 277/2008 Coll., which regulates the categorisation of accommodation facilities and the grading of their classification. The host is responsible for the categorisation and classification of the accommodation facility (premises destined for rent which were originally used for housing, are included in the category: “private accommodation”). When all hygienic requirements for the interior environment, spatial arrangement and functional division, furnishing and operation of the accommodation facilities are ensured, the host must write an operating agenda and submit it to the competent authority (Public Health Authority of the Slovak Republic) for approval (€50). Thereafter, the representative of the Authority visits the facility for the second time and, if everything is in accordance with the rules, approves the operating agenda.

Whereas, in order to ensure hygienic requirements, it is sometimes necessary to invest in the renovation of premises, it is advisable to consult about the operation of the facility with a competent hygienist before renovation. The operation cannot be initiated without the approved operating agenda, preceded by the personal visit of a competent hygienist and physical verification of the requirements directly on the premises of the future accommodation facility. This process can also take from 30 to 60 days. Thus the whole process of compliance with regulations and approval can take up to more than 4 months and cost hundreds of euros. Moreover, the host has to report foreign guests to the Alien Police Department. The host authenticates guests and notes in the guestbook the guest’s nationality,

date of birth, passport number, permanent address and period of stay. In addition, the host must fill out an official form to report the stay of a foreigner and send it to the Alien Police within 5 days.

Finally, a host is required to report his or her activities for accommodation to the tax administrator in the municipality in which the services are provided. A host must complete the form: "The announcement of origin of accommodation". Accommodation Tax is paid for each night that a person stays at a facility. On average it is 0.50-1.50 euro. This is charged on a monthly basis.

The arrival of Airbnb in Slovakia

Airbnb does not command its landlords to have a licence for being self-employed, and also does not require an official change in the use of the construction, connected with additional inspection processes. Similarly, Airbnb does not require official hygienic checks, but relies on the reputation mechanisms of the platform.

Public institutions in Slovakia have not yet officially responded to the presence of Airbnb. This is probably caused by the fact that Airbnb has still not played an important role in the Slovak housing sector. Even the local branch of Airbnb does not have its own manager (except for the Manager in the Czech Republic). In principle, one can only conclude that Airbnb significantly unburdens providers of "private accommodation" of costly regulations.

Recommendations

First of all, it is important to stress that the Slovak government did not prohibit the sharing economy, as many countries did. The Slovak government did not "shoot first, ask questions later". It has, however, not asked many questions thus far, either.

Nevertheless, this is not sufficient. Uber drivers should be freed from taxi licence requirements. Private regulations and reputation mechanisms have transpired to be a more effective way of ensuring the quality of services. The Slovak tax system is also quite hostile to Uber drivers, who are required to obtain a business licence for being self-employed, which is heavily taxed by lump sum contributions after the first year.

Regulations of accommodation services need to be changed as well. Not just because of Airbnb, but also for their excessive burden on traditional providers. There are no reasons to regulate every aspect of the services provided, requiring a change in the use of the construction, to categorise and classify accommodation facilities and finally to write an operating agenda.

LITHUANIA

Taxi regulations

- Special yellow markings on the side of the car
- Light taxi sign on top of the car (€50)
- Registered taximeter and journal logging the entries. (€300 per week)
- Special taxi licence plate (€20)
- Yearly vehicle inspection. Bi-annual, if the car is older than 5 years (€15)
- Taxi driver's certificate (granted after passing a test) (€45 per week)
- Municipal issued licence (20 days €35)
- Civil insurance
- Municipalities may create additional restrictions, such as requirements for the quality of a car, driver's dress code, etc.

Government and Uber

Uber established its Lithuanian headquarters in January 2014. At first, its main purpose was software development. The Government welcomed the arrival of Uber. In fact, the Mayor of Vilnius was the one who invited Uber and urged it to start providing services. Uber drivers started working in November 2015. At first, there were legal ambiguities in terms of regulations. Different institutions interpreted regulations differently, thus making it difficult for drivers to comply with the existing regulations. However, following the Lithuanian Prime Minister's public support of Uber and other examples of the sharing economy, other governmental institutions became more welcoming as well. Even though traditional taxi drivers have expressed concern about the difficult competitive position they find themselves in at the moment, the government remains welcoming towards car-sharing services. Some taxi companies have even taken up Uber's business model and started hiring non-taxi freelance drivers themselves. An Uber driver must have a business licence for an individual activity. The business licence itself is

free, but a person must then pay taxes according to income. The tax payable is 16.6–22.5% of the income earned.

The rise of a new transportation business model urged the government to create a new regulation which is now being deliberated by the Lithuanian Parliament. But it seems that it will not be as strict as the one applied to traditional taxi companies. Two main requirements that are under consideration now are that a company providing intermediary transportation services must hold a government licence and an insurance policy. Government licenses are not difficult to acquire. A person must pass an exam which is held on a weekly basis and must apply for a licence. Additional requirements may be established in post-legislative acts later on.

Regulations of accommodation services

- Licence for providing accommodation services 30 days, free of charge
- Buildings have to be at least 46 dB soundproof
- Temperature must be at least +18°C
- Building must have a secure electricity connection
- Building must be connected to a public telephone network system
- Building must have storage for cleaning supplies, bedding, bed sheets and other items
- Handicap-accessible
- Special security instructions
- Water supply and sanitation
- Fire safety standards
- Lighting and ventilation requirements
- Construction and building planning
- Health inspection. (€44-117, depending on the size of hotel. Issued in approx. 60–70 days)

Government and Airbnb

Even though Airbnb has been providing services in Lithuania for a couple of years now, the government has not addressed this issue. Not long ago, the Lithuanian Hotel and Restaurant Association initiated discussions in the Ministry of Economy concerning the regulation of accommodation platforms such as Airbnb. The discussions are still in the very early stages. It is therefore difficult to state explicitly what type of regulatory regime will ensue. However, it appears that it may be on the rather strict side and force providers of accommodation services to pass certain hygiene,

fire safety and health inspections, similar to those applicable to traditional hotels.

Recommendations

What the regulator should be concerned about is consumer well-being. This means that the old regulatory practices should be reassessed and obsolete requirements should be revised. The market test has shown that passengers do not require special yellow stripes on their transportation vehicles, and tourists do not need exceptionally high fire safety requirements such as those applicable to hotels. A level playing field for different businesses should be created by getting rid of outdated regulations that consumers have shown to be excessive.

THE CZECH REPUBLIC

Taxi regulations and Uber

The Czech regulations differentiate between two types of transport services: taxi service and car-sharing /carpooling.

Taxi: Taxi service is defined by the Road Transport Act (111/1994) as an activity based on transport services provided to a maximum of 9 customers, regularly and for profit. The activity is provided under a special taxi concession. To become a taxi driver, one has to take 4 steps: obtain a taxi driver's ID (500 CZK/20 EUR), pass a taxi driver's exam (topography, legislation, taximeter operation), register the car as a taxi (fee 100/500 CZK; 4/20 EUR), and acquire a Trade Licence in the form of a taxi concession (2000 CZK/75 EUR). The driver must also have special responsibility insurance for any customer issues during the transport (called Seat Insurance).

Car-sharing/carpooling: Car-sharing is defined as a short-term car rental (without driver). One may ignore it, because Act 111/1994 Coll. does not apply here. Carpooling is defined as a contract based on Civil Code (89/2012 Coll.), which is not provided primarily for customers' utility – a carpool driver satisfies the own needs to drive him- or herself from place A to place B and another individual with the same transport needs just shares the costs with the driver. According to the regulation, carpooling is not a taxi service (it should be the driver who determines the destination), nor an economic

activity (it should not be a profit-seeking activity, but a cost-sharing activity).

The controversy of the sharing economy in transport mirrors the legal dispute over the regulative requirements which apply to taxi drivers and not to carpool drivers. Currently, the discussion about the legality of carpooling applications (UberPop, for example) has two bases – the Road Transport Act and the Trade Act. According to the Road Transport Act, the key component of the service is the question: “Whose need is satisfied?” If it is taxi transport, the customer decides where to go and the driver satisfies this need in exchange for money. If it is a carpool, the driver decides where to go and the passenger shares the cost. The factor of choice of final destination is used as a key argument against carpooling companies in the Czech Republic. According to the Trade Act, economic activity is defined as a permanent activity which is provided individually, in own name, on own responsibility and with the aim of generating a profit. The factor of “mercenary purpose” is a key argument used against carpooling companies in the Czech Republic.

Services provided in the Czech Republic:

Liftago: The application operates as online dispatching for professional taxi drivers, no legal disputes here.

WunderCar: Carpooling application. Argument against by critics is based on “voluntary” customers’ opportunity to pay the driver. There is a discussion about the legality.

Uber Black: Application operates as online dispatching for professional taxi drivers. Controversy is based on a dispute between Uber (“this is non-contract transport, so one does not need taximeters or taxi identification”) and critics (“this is contract transport, your drivers must have taximeters and taxi identification”).

Uber Pop: Carpooling application defined as “carpooling on demand”. A customer actively asks for a carpool drive and waits for the Uber Pop driver to collect him or her at the stated spot and drives him or her to the requested destination. Communication is completely carried out via mobile application. This service is the most controversial

one; critics say Uber drivers provide a regular taxi service without any licence, trade licence or concession. Moreover, some critics say that the maximum taxi price cap (28 CZK/km; 1 EUR/km) is exceeded in some cases by Uber Pop drivers. Uber states it is just a carpool and one needs no licence for carpooling. And there is no price cap on carpooling. Uber also argues that Uber Pop drivers use the platform less than 20 hours per week, so they are not professional drivers.

The tax obligation is fully transferred to drivers. In the Czech Republic, the legislation defines an occasional income as a random activity which generates unsystematic revenue no higher than 30 000 CZK/1 100 EUR per year. Critics state that this is not the case for Uber Pop – drivers intentionally install the application with a business goal. According to tax advisors, Uber Pop drivers should pay regular income tax – their activity is a continuing business activity, so a driver can deduct costs from his gross income (eligible real costs or proportional costs), but both tax and social security obligations must be adhered to.

There is also an intensive discussion on the Value Added Tax obligation. Critics state that Uber is an economic subject registered in the Netherlands and drivers, as economic entities, receive the service (Uber platform) from abroad. Therefore, they should pay VAT from Uber commissions, similarly to persons who advertise through Google AdWords.

All these issues are under serious discussion among lawyers, officials, taxi drivers’ lobbies and Uber defenders.

Accommodation regulations and Airbnb

According to the Czech regulation, one can provide accommodation in one’s own property under two regimes – economic accommodation activity (under the Trade Act) or rental activity (under the Income Tax Act). The first regime requires a Trade Licence (accommodation services), which means the activity is provided regularly, on an accommodation contract basis (may be verbal) and with the purpose of profit-seeking. The second regime is based on a short-term property rental contract – an individual does not need any Trade Licence, but the income should be taxed under §9 of the Income Tax Act (income from rentals). One

should also have an agreement with the property owner, if the property does not belong to him or her.

Last but not least, one should ensure that foreign guests have been registered in the Alien Police database, or they must do it themselves. Legislation states that anyone who comes to the Czech Republic from a non-EU state for more than one day or from a EU state for more than 30 days, must register the stay at the Alien Police or do it through an accommodation provider. Therefore, the provider should administer a guestbook and provide the information within three working days.

Critics of sharing economy accommodation services – especially interest groups represented by hotels and restaurants – state that these services extend the shadow economy (tax evasion), do not follow hygiene regulations or accommodation standards and also do not follow the Alien Police reporting regulation. Nevertheless, in the Czech Republic, this discussion is more modest in comparison with the sharing economy transport services.

BULGARIA

The traditional sectors for providing accommodation and taxi services in Bulgaria are subject to substantial regulations, which translate into lengthy licensing procedures and serious costs upfront.

Regulation of taxi services

Taxi services can be performed either by a licensed transportation company, which has been registered for the operation of passenger taxi transport, or by a legal person, acting on its behalf but on its own account. The latter practice is more widespread in Bulgaria – taxi drivers are registered as sole proprietor companies, acting on behalf of a bigger company for taxi services. The taxi company typically leases out cars to drivers, and maintains a dispatching service.

If a licensed transportation company wishes to offer taxi services, it needs to:

- register with the Automobile Administration executive agency (at the Ministry of Transport) for the operation of taxi transport of passengers;
- equip each future taxi car with a meter, which

has a so-called fiscal memory (i.e. a cash machine);

- obtain permission to operate a taxi service within a given municipality by the Mayor; the permission is applied for and issued for each car the company plans to use.

Those two procedures and the taxi meter cost a total of about BGN 450-850 (EUR 230-435). The exact sum depends on the municipal fee for the permission to operate a taxi service, as well as on the market price of the taxi meter.

Apart from the above-mentioned registration and permission (i.e. licensing) regimes at the central government and local government levels, respectively, the State's regulation of taxi services extends to the taxi driver and the car, too. The car should be no older than 15 years, and have meters, visible signs of the Transportation Company, as well as visible stickers with their tariffs. The driver, in turn, should be no younger than 21 years of age (even if a driver's licence can be obtained at 18), and have valid documents proving he or she is physically and psychologically healthy, and has not been sued in the past. Also, taxi drivers, like all other drivers, should have a valid civil liability insurance (against third-party damage).

It is noteworthy that local authorities, apart from licensing taxi companies that are allowed to operate on the municipality's territory, regulate taxi companies in another important aspect. Local municipal councils set the minimum and maximum prices of taxi journeys for their municipality, which makes taxi services one of the heaviest regulated businesses in the country.

Regulation of hoteliers

In order to start an accommodation business, one needs to file for categorisation of the would-be-hotel or any other type of accommodation. The hotelier has to submit 9 different documents, including copies of certificates showing the qualification, language and professional training of all (future) staff and the Hotel Manager (!).

The categorisation procedure applies to all types of accommodation, including traditional hotels, family hotels, guesthouses and rooms to let. However, guesthouses and rooms to let are subject to less stringent regulations, as their categorisation

requires fewer documents – a certificate showing that the hotelier is registered in the company register; a form for categorisation; a copy of the title of ownership or rent contract; a receipt showing that the fee for categorisation has been paid.

The whole procedure can take up to 4.5 months – 15 days for a review of the documents for flaws and omissions, and then up to 4 months for the actual categorisation process, including an on-site visit by government experts. The fee for categorisation varies between BGN 250 and 5000 (EUR 128-2556), depending on the type of accommodation (e.g. hotel, guesthouse, etc.) and the number of beds available. Once categorisation is obtained, the accommodation facility has to be registered on the National Tourism Registrar, which costs another BGN 150 (EUR 77).

Public institutions' reaction to the emergence of sharing economy businesses

Uber has thus far been the only large and recognisable sharing economy business to have set foot in Bulgaria. The company started operations on 9 December 2014, with the launch of its low-price UberX service in the capital city of Sofia. Nevertheless, its operations in Bulgaria lasted less than a year, ending in the autumn of 2015. By that time, Uber had some 40 000 clients in the capital, and had also recruited 20 software engineers for its software development centre. The latter was one of 5 such centres worldwide and the company had publicly announced plans to triple its staff by the end of 2016.

The reason for the termination of Uber's operations in Sofia was the decision of the Commission for Protection of Competition (CPC) that Uber had violated the Bulgarian competition law. Thus, the anti-trust commission imposed a fine of BGN 200 000 (approx. EUR 102 258) on Uber and ruled for the immediate cessation of its operations in the country. The decision of the CPC was appealed before the Supreme Administrative Court, but the latter confirmed it. The main argument of the Commission was that the UberX service was not a form of shared travel service, because it is not free of charge (in contrast to shared travel platforms, which are).

Along the same line, in April 2016 the Minister of Transport appealed for the ban on all local sites

offering shared travel. His position was declared after a meeting with the national association of bus transportation companies, which regard those sites as a tool for unfair competition from companies operating in the shadow economy. Indeed, such sites are often used by businesses which offer the same, regular transport services in parallel to licensed transport companies, but at lower prices. Nevertheless, the emotional response of the Bulgarian government appears to be rather short-sighted.

Policy recommendations

In contrast to just banning such sites (which, by the way, would swallow a significant amount of taxpayers' money to monitor and control), the government could follow the approach of some more open-minded regulators in Europe and the USA. The sharing economy has been booming in North America and Western Europe in the past 5-6 years, where forward-looking regulators have adapted existing regulations and tax laws to suit these new forms of economic relations. Moreover, smart regulators have tried not to stifle the development of sharing economy practices, but rather to encourage their expansion with parsimonious regulations, tax exemptions (e.g. for rent income below a certain limit) and equal treatment of newcomers to traditional businesses. If existing regulations of e.g. taxi or accommodation businesses impose significant compliance costs, then the better approach is to seek a reduction of those compliance costs in order to create positive incentives for operations in the formal economy. Sanctions and bans, i.e. negative incentives, have been proved to render worse results in terms of compliance if the institutional environment is weak – as it is in Bulgaria.

5. Conclusion

First of all, it is important to recognise that one has to compare real public regulations with real private regulations. Neither of them is perfect. However, as was shown above, creators of private regulations are owners and it is in their self-interest to create as effective regulations as possible. This does not hold for public regulations.

It is also important to recognise that, although individual sharing economy platforms compete with companies from various traditional sectors, it does not follow that they should be regulated by existing public regulations. Rather than trying to force new technologies to submit to old existing regulations, existing public regulations should be adapted to current developments.

The approach to “shoot first and ask questions later” being used by various (local) governments is even worse. It not only cuts off current customers and suppliers from the mutually beneficial exchange, but it creates high costs and barriers to entry into the markets (not everyone can afford to pay lawyers and fines to get their representatives out of prison). Hence, governments by their incorrect approach to the sharing economy can create monopoly problems in the future (which will then require other interventions and thus trigger a spiral of interventions).

Furthermore, this approach cuts off the whole of society from the future potential of new technologies and solutions to all kinds of problems, needs and requirements. Thus, society faces the risk of slowing or negatively affecting the development and enormous potential of this new branch of the economy.

There are 6 principles which should be followed when creating or re-evaluating public regulations of the sharing economy:

- 1) New regulations should not limit choices for customers and service providers within the sharing economy;
- 2) New regulations should support the sharing economy’s strong points – flexibility, decreased transaction costs, employment, employment of marginalised population groups, identification of bad public regulations;
- 3) The playing field should be levelled towards fewer regulations; it should lead to liberalisation of existing public regulations;
- 4) Public authorities should set clear and simple rules assigning responsibility for safety and apply them equally to all platforms and traditional service providers. This means that entrepreneurs should be held liable for potential harm to consumers, but legislation should not try to prescribe detailed solutions. There should be space for innovative answers to the problems;
- 5) The EU should develop a guideline to best practices on how to react to the sharing economy. The EU should focus on making sure that states do not violate basic rules – open competition and free movement of goods, services, people and capital;
- 6) The possibility of tax compensation for traditional sectors, which were forced to bear the cost of public regulations so as to mitigate their opposition, should be reconsidered.

The sharing economy is an opportunity for everyone. Do not get it wrong. There will be losers. Like every innovation, the sharing economy threatens traditional ways of doing things. So how can one be sure that there will be more winners? The main reason is that this change is taking place through a chain of voluntary exchanges. The voluntariness is the ultimate test of net benefits for society. Hence, the sharing economy is a threat to some, but an opportunity for everyone.

TAXI DRIVERS REQUIREMENTS

	Slovakia		Czech Republic	
	Financial costs	Time/papers needed	Financial costs	Time/papers needed
Trade Licence	5-10 euro	3 days	N/A	N/A
Demonstrating financial standing	1000 euro / 1 car	A certified statement of assets and liabilities	No	No financial statement needed
Age of the car	N/A	Not older than 8 years when registred	No	Standard technical certificate
Licence Deed	30 euro	31 days	1000 CZK	30 days
Driving experience	N/A	Min. 3 years	No	Standard driving licence
Mandatory medical examinations and psychological tests	60-80 euro	N/A	No	Nothing like this needed
Parking spots	500 euro / year (not obligatory)	Renting contract	No	Nothing like this needed
Driver's licence taxis	50 euro			
Professional competence test	50 euro	Passing the special exam (it takes place only once every three months and there are only 20-50 free places)	No	Passing a special exam
Seminar before competence of taxis (facultative)	65 euro	N/A	No	Nothing like this needed
Taximeter	400 euro	Must have a printer	11000 - 17000 CZK	Taxis have it, carpooling services do not have it
Liability insurance cover for work-related damage	120 euro / year	N/A	?	Taxis must have it, it is usually a part of compulsory insurance
Visual taxi signs on cars	70 euro	N/A	500 CZK	Yellow sign TAXI, so called "hat"
Yearly vehicle inspection	60 euro	Every year	N/A	N/A
The obligation to undergo a medical examination every five years and after the 65 years, every two years	N/A	N/A	200 - 500 CZK	No special examination for taxi drivers, but drivers older than 65 yrs must visit a doctor every two years

Note: 1 EUR = 27 CZK, 1 EUR = 2 BGN

Bulgaria		Lithuania	
Financial costs	Time/papers needed	Financial costs	Time/papers needed
450-850 BGN	2 different procedures - one for registration of the company as a taxi transportation company (with the automobile administration agency), and another one - for receiving a licence for taxi transportation (from the municipality). The total time is about 3 weeks for both procedures.	N/A	N/A
N/A	Statements of assets and liabilities	N/A	N/A
N/A	Not older than 15 years	N/A	N/A
N/A	N/A	€ 35	20 days
N/A	No requirements for years of driving experience, only a licence for taxi; there is also an age requirement for the taxi driver - min. 21 years.	N/A	N/A
Around 25-60 BGN	Documents of medical evidence proving that the driver is physically healthy and psychologically stable	N/A	This examination does not differ from a traditional driving examination
N/A	N/A	N/A	N/A
115 BGN	No, just the standard driving licence is sufficient	€ 45	1 week
N/A	No	N/A	N/A
N/A	Yes, with fiscal memory	€ 300	1 week
Between 150 and 1000 BGN	Price depends on the years and engine of the car, the age of the driver, etc.	N/A	N/A
N/A	There should be a visible sign that shows the car provides taxi services	May vary depending on the service provider. At least a €100	N/A
N/A	N/A	15	Yearly vehicle inspection. Bi-annual if the car is older than 5 years
N/A	Term of validity of medical document proving psychological stability - 3 yrs, for those above 65 years of age - 1 year.	Municipalities may create additional restrictions such as requirements for the quality of a car, driver's dress code etc.	N/A

HOTELIERS REQUIREMENTS

	Slovakia		Czech Republic	
	Financial costs	Time/papers needed	Financial costs	Time/papers needed
Trade Licence	5-10 euro	3 days	N/A	Airbnb rentals are mostly provided under the Income Tax Act (no Trade Certificate needed)
Construction type reclassification	30 euro	Needed documents: construction permit, construction drawings, ownership document, copy of cadastral map. It takes 1-2 months	N/A	Agreement with a property owner (if the property is not yours)
Submit for approval to health authorities, firefighters and construction office	50 euro	Comply with hygiene and fire rules	N/A	N/A
Ensure hygiene requirements	50 euro	Define the category and class of accommodation. A room must meet the minimum requirements: e.g. a glass of water, a desk, a wardrobe, a mirror etc.	N/A	N/A
Prepare the operating instructions of accommodation	N/A	It takes 1-2 months	N/A	N/A
Report guests to The Alien and Border Police	N/A	Host has 5 days to report	N/A	Host has 3 days to report a non-EU state guest staying for more than one day or EU state guest staying for more than 30 days
Rental income tax to the Local Government	0,5 - 1,50 euro / overnight stay	The local government sets tax rates for the overnight stay	N/A	Local governments can impose a local tax (spa/recreation fee) for overnight stay in maximum amount 15 CZK/day. Airbnb host should inform her/his guests that the fee is included in the final price.

Note: 1 EUR = 27 CZK, 1 EUR = 2 BGN

Bulgaria		Lithuania	
Financial costs	Time/papers needed	Financial costs	Time/papers needed
N/A	Papers: Licence for categorization of a hotel	N/A	N/A
From 250 to 5000 BGN, depending on the type of accommodation and number of beds	Up to 4,5 months - the review of the documents above takes up to 14 days and then the procedure for categorisation, including an on-site visit, can take up to 4 months.	Licence itself is free, but the compliance with the requirements may be tricky. 30 days	Buildings have to be at least 46 dB soundproof, temperature must be at least +18, building must have a secure electricity connection, building must be connected to a public telephone network system, building must have storage for cleaning supplies, bedding, bed sheets and other things, handicap-accessible, special security instructions, water supply and sanitation, fire safety standards, lighting and ventilation requirements, construction and building planning
150 BGN	For registering of the hotel in the National Tourism Registrar, after the former has been categorised	N/A	N/A
Around 50 BGN	Follow the rules listed for fire installation and hygiene	€17-44 depending on the size of a hotel	60-70 days
Around 50 BGN	Following the minimum hygiene and sanitary requirements. Preparing the accommodation and the facilities in the rooms in tune with the normative requirements for each hotel category	N/A	N/A
Depends on the category	Send regular reports on foreign tourists to the ministry of interior	N/A	N/A
Between 0.5 and 1.5 BGN per overnight stay	It is up to the local government to define the amount of the so-called tourist fee	N/A	Municipalities may apply additional "pillow" tax

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Notes:



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