

Risk Management Implications of the Sharing Economy

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The sharing economy is rapidly growing in the number and types of services being provided. Its dynamic and ever-changing nature, as well as the diversity of services and locations across the United States and in many other countries in the world, has created much confusion over regulation of the industry and insurance requirements of the parties involved.

Two of the largest segments of the sharing economy are ride sharing and short-term housing rentals. These two segments also account for the majority of reported insurance and regulatory issues. Accordingly, this paper will limit its focus to these two segments, the State of California in particular, and to the identified property-casualty risk management and insurance issues.

Introduction to the Sharing Economy

The *sharing economy* (also referred to as the *share economy* or *shared economy*) is a form of collaborative consumption built on a foundation of technology. It allows individuals to share owned assets that they do not fully use. While the idea of barter is normally associated with traditional nonmonetized economies, it continues in more modern economies. There are long traditions of informal bartering. Most of these deal with exchanging time, labor, or skills.

For example, an accountant might trade tax-return preparation for a plumber's installation of a new water heater. Babysitting cooperatives among young families (some with very elaborate rules and regulations) have existed since urbanization began. Other bartering situations deal with assets—for example, car pools, or shared vacation homes. We can all think of cases when we have given time, shared a tool, borrowed a couple of eggs from a neighbor, or prepared a meal for someone who was ill, knowing that a like service would be rendered, as needed, in the future.

What differs in the new and emerging sharing economy is the widening of sharing groups to include strangers and a return to monetized sharing of assets (or occasionally time/labor) through the use of high-tech production platforms provided by for-profit sharing network companies (SNCs) that match buyers to sellers through the Internet and through mobile apps available on smartphones and tablets. These companies often provide certain guarantees in terms of payment and delivery of services, protection from damage to shared assets, and transparency through the facilitation of open reviews of buyers and sellers. Payment is made through the SNC for services rendered, and the SNC retains a portion of the payment made between the sharing parties.

There have been ongoing deliberations regarding the impact of SNCs on the competitive structure of existing markets as well as to claims of regulatory arbitrage and tax avoidance. This has led to legal and regulatory challenges and legislation, going to the heart of the sharing economy and of insurance issues, in particular. These actions are taking place across the United States and in some instances, around the world. As a review of all of these is beyond the scope of this paper, we concentrate on the process in California, where most of the SNCs were founded and where the regulatory and legislative processes are now well advanced.

Many SNCs initially claimed there was no legal difference between the services that they provided and those provided by traditional information-sharing services (ride boards, vacation rentals in newspapers, Craigslist postings, etc.), and that their responsibility should be no different. Notwithstanding, when SNCs retain a portion of the payment from the user before transferring payment to the owner, they may be construed to be providing a brokerage service with corresponding legal, tax, and insurance consequences. Many of the SNCs that are

discussed in this paper are becoming aware of the implied legal responsibilities and are, in a measured way, in the process of expanding insurance coverage or of offering providers and users of shared assets more complete risk exposure information in response to the evolving regulatory environment.

SNCs were innovative in recognizing the economic inefficiencies and began building technological platforms to turn underutilized assets into profits. There is an excess of privately owned cars, but a lack of parking spaces (JUST PARK, PARK ON MY DRIVE). Individuals may own vacation homes or spare bedrooms that they do not fully use (AIRBNB, HOMEAWAY/VRBO). An individual may own a car that can be used to provide on-demand transportation services (UBER, LYFT, SIDECAR); many of the firms that facilitate these services have been highly successful. For example, in June 2014, analysts calculated that the market valuation of UBER was close to \$17 billion based on the upside potential expanding beyond current peer-to-peer transportation services.¹

Several of the SNCs, particularly those that provide taxi-like services or property rental services, are mired in controversy. Regulatory and tax authorities have questioned their business models and whether these services should be allowed, especially when they are competing with existing regulated services. In some cities, such as San Francisco, objections have been raised that rental properties are being illegally sublet, or that the growth of short-term rentals are exacerbating an already tight property market. Homeowners associations are worried about security and the violation of association rules, and lenders that restrict lending to developments that have less than a fixed percent of rentals question whether lending guidelines are being violated.

Historically, innovation and the impact to the status quo have been in conflict. Direct competitors, including the taxi and hotel associations and unions, are raising major challenges. At the same time, the individuals with underutilized assets, the SNCs, and the consumers participating in the sharing economy are all expressing their support for the newer technologies.

¹ Knowledge@Wharton, "Kicking the Tires on Uber's \$17 Billion Valuation: Is It Worth That Much?", July 16, 2014, <http://knowledge.wharton.upenn.edu/article/kicking-tires-ubers-17-billion-valuation-worth-much/> (accessed November 25, 2014). The reported estimate is based on \$1.2 billion in funding in June 2014.

In the midst of these challenges to traditional concepts of asset utilization and accompanying risks, the new technologies introduce challenges for the insurance industry. The innovations create risk management issues that are different from more familiar resource allocation. Some of the sharing practices may be in violation of the terms and conditions of personal and commercial insurance policies that are purchased by the participants in the sharing economy. The expectation of insurance protection may be at odds with what is ultimately afforded.

This is the challenge to be addressed in the following sections.

Ride sharing in a Sharing Economy

“That electronic thumb replacing the one waving by the side of the road. That’s it, really, that’s all they are...” – Jim Worstall²

The development of ride-sharing arrangements has presented significant technological, legal, regulatory, and risk management challenges in the sharing economy. Technological platforms enable real-time linkage of supply and demand for transportation needs, connecting individuals who are willing to provide transportation services with individuals seeking those services.

There is tremendous heterogeneity in the supply market. Some individuals provide ride sharing on a very part-time basis, during commuting hours to pass through toll lanes, or occasionally generating additional income after work or school and on weekends. Others provide ride-sharing services on a close to full-time basis. This heterogeneity underlies the challenges for insurers that are addressed in this chapter. Moreover, the sharing economy associated with ride sharing created a direct challenge to traditional providers of transportation services—taxis, limousines, and other livery services. This has resulted in legal challenges, regulatory challenges for public-utility regulators (and insurance regulators), and challenges and opportunities for the insurance industry.

While this paper outlines some of the legal and regulatory issues and challenges (with a focus on California), it concentrates on the underlying insurance and risk management challenges for the ride-sharing companies, the individuals providing and using ride-sharing services, and the general public (even if not engaged in ride-sharing).

History of Ride Sharing

Ride sharing is not a new concept. Carpooling is decades old in California. Ever since the 1973 oil crisis, the rising cost of transportation forced people to seek alternative methods to reduce transportation costs. Casual car pools developed and often consisted of informal

² Tim Worstall, “This Is Why We Can’t Have Nice Things: Uber and Lyft Drivers Being Arrested,” *Forbes*, August 3, 2013, www.forbes.com/sites/timworstall/2013/08/03/this-is-why-we-cant-have-nice-things-uber-and-lyft-drivers-being-arrested/ (accessed November 25, 2014).

locations at which drivers and passengers could meet without prior arrangement. Costs were shared informally. Websites were developed to provide location sites and propose etiquette. Discussion boards were set up to share experiences and make suggestions.³

Technological advances including GPS navigation devices, smartphones, and expanded social networks made real-time ride sharing and the development of ride-sharing companies possible. These companies developed in the context of aging and inadequate public-transit systems that lacked availability, and in some cases, in the perceived low quality of taxi/livery services. Competing with the taxi industries, these companies advertise advantages including availability without the need to pay in cash.

Transportation Network Companies,⁴ or TNCs, previously referred to as ride sharing or ride-share companies, are part of a new generation of companies included in the sharing economy. Three of the prevalent TNCs are Uber/UberX, Lyft, and Sidecar. While each follows a slightly different business model, each is similar in that:

- Drivers are considered independent contractors who contract with the TNC to obtain information about ride-sharing customers and serve as a conduit of payment for ride-sharing services.
- Each TNC has a proprietary application that the user downloads and accesses using a smartphone or tablet.
- These applications all utilize GPS navigation to connect drivers with passengers and to monitor the distance driven to determine the fare.
- Drivers and passengers each have the opportunity to rate each other anonymously after the ride. This helps reduce information asymmetries regarding driver quality and knowledge of routes, cleanliness of car, etc.

³ As an example, RideShare, the Metropolitan Transportation Administration's website, created an interactive network to support that carpooling benefits drivers by reducing transportation cost and helps the environment by reducing traffic, pollution, and the consumption of scarce resources, www.ridematch.511.org.

⁴ The California Public Utility Commission (CPUC) created the terminology Transportation Network Companies (TNCs) to describe ride-sharing companies. This term is being used elsewhere, but is not universal.

*Transportation Network Companies*⁵

Each of the three major ride-sharing firms was founded in San Francisco within the last five years. Each began by developing technology-based platforms to connect drivers with riders and rapidly grew into multimillion-dollar businesses making incredible profits.

Lyft was the first of the ride-share companies to start operations. In 2007, Logan Green and John Zimmer initially created the ride-sharing company Zimride, which focused on connecting passengers and drivers making longer trips through Facebook Connect. In July 2013, Zimride was sold to Enterprise Holdings, parent company of Enterprise Rent-a-Car. This transaction allowed Green and Zimmer to concentrate on Lyft⁷. Lyft's slogan, "your friend with a car," and the founders' signature pink mustaches helped brand the vehicles.

Uber was founded by Garrett Camp and Travis Kalanick as Ubercab in 2009. Their mobile application instantly connected passengers with professionally licensed drivers of vehicles for hire. In 2010, Uber announced its plans to expand ride sharing to non-taxi vehicles under the UberX name while retaining the higher-level service under Uber.⁸ Drivers who signed up for the UberX mobile application could be matched with

Major Transportation Network Companies

Lyft

Cities: 68 in the United States

Drivers: More than 60,000

Venture Financing: \$333 million

Uber

Cities: 70 worldwide

Drivers: Not disclosed

Venture Financing: More than \$1.5 billion

Sidecar

Cities: 9 in the United States

Drivers: 6,000

Venture Financing: \$20 million

Source: Singer N. (2014, Aug. 17). New York Times.

⁵ Information in textbox extracted from Natasha Singer, "In the sharing economy, Workers Find Both Freedom and Uncertainty", *The New York Times*, August 16, 2014, www.nytimes.com/2014/08/17/technology/in-the-sharing-economy-workers-find-both-freedom-and-uncertainty.html?_r=0 (accessed November 25, 2014).

⁷ Ken Yeung, "Lyft Founders Sell Zimride, Their Carpooling Startup, to Enterprise Rent-a-Car's Parent Company," *The Next Web*, July 12, 2013, <http://thenextweb.com/insider/2013/07/12/lyft-founders-sell-zimride-their-carpooling-startup-to-enterprise-rent-a-cars-parent-company/> (accessed November 25, 2014).

⁸ Alexia Tsotsis, "Uber Opens Up Platform to Non-Limo Vehicles With 'Uber X,' Service Will Be 35% Less Expensive," *TechCrunch*, July 1, 2012, <http://techcrunch.com/2012/07/01/uber-opens-up-platform-to-non-limo-vehicles-with-uber-x-service-will-be-35-less-expensive/> (accessed November 25, 2014).

customers using the application or by text message. Later developments included the ability for customers to track the reserved car.

Sidecar was founded in February 2012 by Sunil Paul and Jahan Khanna, who wanted to provide a new option for personal transportation.⁹ Their smartphone application initially facilitated drivers offering a ride with alerts to ride-share requests. Sidecar's updated application allows drivers more flexibility in setting individualized market-based fares, including increases for large numbers of passengers, distance, and pick-up or drop-off areas. The application also offers the ability to combine passengers traveling to the same area.

Currently, **Uber** operates globally, while **Lyft** and **Sidecar** operate only in the U.S.

Controversies

"The mustache wars are on", says Jon Brooks of KQED in his three-part series, *Will Ride Sharing Kill San Francisco's Taxi Industry?*¹⁰ The taxi companies are protesting because they are held to tight regulation and deem the unregulated ride-share companies as unfair competition. Most cities in California regulate the taxi industry, which includes licensing, training, rates, insurance, and permit fees. Members of the United Taxicab Workers and similar organizations across the country claim they will be ruined, and the lack of TNC regulation will impact public safety.

In response to these challenges, Uber, Lyft, and Sidecar initially claimed to differentiate themselves from the taxi industry based on their ride-sharing applications technology. Lyft and Sidecar describe their applications as "the digital equivalents of a break-room bulletin board that brings together strangers who want to carpool," while UberX claims it only "links customers with a service, like a restaurant reservation app."¹¹ Notwithstanding, incidents such

⁹ Market Wired, "SideCar Connects Drivers and Passengers One Ride at a Time," Yahoo! Finance, June 26, 2012, <http://finance.yahoo.com/news/sidecar-connects-drivers-passengers-one-131500215.html> (accessed November 25, 2014).

¹⁰ Jon Brooks, "California Bill Would Enable Uber, Lyft Drivers to Finally Get Insurance," KQED News, September 2, 2014, http://blogs.kqed.org/newsfix/09/02/2014/Uber_Lyft_California_insurance/ (accessed November 25, 2014).

¹¹ Daniel C. Vock, "State Regulators Step In on Ridesharing Controversies," *Stateline*, October 10, 2013, www.pewtrusts.org/en/research-and-analysis/blogs/stateline/2013/10/10/state-regulators-step-in-on-ridesharing-controversies (accessed November 25, 2014).

as an Uber driver killing a six-year-old pedestrian on New Year's Eve (see box) raised questions regarding insurance coverage and exposure of the TNCs.

Public concern, partially stoked by the taxi industry's fear of competition, was voiced in the media. Concern included the safety of passengers; pedestrians; other property, including other vehicles; and the driver. These concerns led to questions regarding the adequacy of insurance and potential coverage gaps. As a result of regulatory pressure, all three have started to provide commercial insurance coverage, described as excess of a driver's personal automobile policy with a drop-down provision in case the primary insurer denies coverage.

The reliance on personal automotive policies (PAPs) as primary protection is problematic. Numerous insurance experts have pointed out that ride-share drivers who rely on personal automobile policies for primary protection may void their coverage, as policies generally exclude commercial activities and specifically exclude the use of a car in livery services (collecting a fare).

Risk Exposures

Providers of transportation, regardless of the conveyance, have responsibilities for the safety of passengers, pedestrians, and others. TNCs share many of the same exposures to losses that are inherent in traditional public transportation and the taxi industry:

NEW YEAR'S EVE ACCIDENT KILLS

SIX YEAR OLD | UBERX DRIVER

The issues surrounding the lack of regulation was brought to the forefront after a 2013 New Year's Eve accident resulting in the death of a six-year-old and injury to other family members when a car driven an UberX driver turned right at a red light hitting the plaintiffs who were crossing the street in a crosswalk. The plaintiff's lawyer claims that at the time of the accident the UberX driver was operating his vehicle using the UberX app and that he was interacting with it and/or using the UberX GPS at the time of the accident.

Plaintiff lawyer's claims: (1) the driver was an employee of Uber or there was an agency relationship; (2) the interaction with the app was related to the driver being distracted; (3) that Uber would be responsible for all claims that exceeded their commercial excess insurance coverage.

Initially there was also a questions raised by the driver's primary insurer of whether there would be coverage under the PAP as it contained a prohibition against providing taxi or livery services. At the time of writing the liability suit is still working through the legal system and the issues have not been fully resolved.

News reports indicated that the primary insurer had agreed to cover losses up to its full level of liability.

Source: K. Williams & K. Alexander.
www.SFGate.com 1/28/2004.

Third-Party Liability or Property Damage Exposures:

- Bodily injury to passengers and pedestrians (including possible lack of uninsured or underinsured motorists coverage)
- Loss to property, damage to other vehicles or nearby structures or utilities
- Criminal acts, including robbery or theft, assault and/or battery (physical or verbal threats), or sexual molestation
- Personal injury, including discrimination or alleged wrongful detention

First-Party (Driver) Exposure:

- Potential bodily injury to driver from an accident or assault, either physical or verbal, or both
- Increase in hazards, including driving around populated areas, accruing additional mileage, or adopting aggressive driving practices when trying to get to a passenger first
- A rise in motor vehicle violations
- Wear and tear or damage to the ride-share vehicle

All of these risks are increased with the amount of time behind the wheel, the time/location of ride-sharing services and the level of driving distractions created from interacting with the app.

There is an additional risk if the driver is severely injured while in the course of responding to the application or driving a passenger, for it may not be clear who will bear the liability. The TNC contracts explicitly state the drivers are independent contractors, which may or may not be within workers compensation statutes.¹² Whether the driver holds an employee versus independent contractor status is the subject of current litigation in several jurisdictions.

¹² Community Enterprise Law, "Independent Contractors and the Next economy," 2014, <http://communityenterpriselaw.org/independent-contractors/> (accessed November 25, 2014).

Risk Exposures Faced by the TNCs

The TNCs face both direct and vicarious liability related to their management of the technology platform. These exposures include:

- Potential for being held vicariously liable for injuries to third parties, including assault or sexual abuse by a driver that has been prescreened, or to its drivers from passengers that have been prescreened
- Potential liability associated with accidents or injuries resulting from poor maintenance of TNC vehicles
- Changes in laws or regulations that interpret the TNCs relationship with drivers as employees, as opposed to independent contractors, with respect to providing workers compensation coverage and being liable for the actions of employees
- Possible product failure resulting in bodily injury or property damage (for example, the app may not be updated for road closings or construction—or for an area that is currently subject to riot or civil commotion)
- Possible privacy breaches and resulting financial losses or identity theft, including the potential for the app to be used as a gateway to other stored private information on the user's mobile device
- Patent infringement
- Libel or slander (resulting from disparaging reviews of drivers or passengers), or the wrongful termination of driver or passenger privileges
- Potential for claims resulting from false or misleading advertising, including misrepresentation to drivers regarding the efficacy of coverage provided by personal automobile policies as primary insurance and/or encouraging drivers (directly or indirectly) to file claims that occurred while providing ride-sharing services to their personal automobile insurance provider
- Claims against directors and officers (D&O) based on mismanagement
- Operating as unregulated entities, in violation of laws, statutes, or local ordinances
- Not collecting and forwarding required taxes to taxing authorities
- Errors and omissions (E&O)

Insurance Issues

Probably the most important issue surrounding TNCs involves legal liability and insurance coverage. The 2013 fatal accident on New Year's Eve and the September 2014 incident of assault with a deadly weapon brought to light the very real concern for gaps in insurance coverage for TNC drivers.

Taxi companies must carry livery insurance at a significant expense. In San Francisco, for example, authorized taxis are required to provide \$1,000,000 liability coverage per incident. Similar requirements exist in other large cities in California and across the nation. Taxi companies are required to provide workers compensation insurance for their drivers, with an estimated cost of \$8,000 to \$10,000 per driver. TNCs' contractual agreements, stipulating responsibilities, differ from one to the other. The absence of standard insurance coverage requirements contracts makes comparisons of coverage difficult.

The TNC Driver's Insurance

There are several critical issues that arise out of the blend of a PAP purchased by the driver and the excess liability policy (with drop down to primary) provided by the TNC.¹³ It is not clear that the independent driver's insurance policies provide liability and/or physical damage coverage sufficient to cover injury to passengers, drivers of other vehicles, or pedestrians.

Among the issues are:

Bodily Injury and Property Damage Liability

Of significant concern is that the driver's PAP coverage will be insufficient or may be voided by ride sharing activities. The TNCs require drivers to verify that their PAP coverage meets a state's minimum coverage levels for personal insurance; however, that level of coverage is a fraction of the \$750,000 required for a commercial livery policy in California (up to

¹³ Initially the TNCs operated with only a requirement of a PAP. This was later changed to the addition of a \$1.0 million excess line of commercial insurance (with the drop-down provision) only when there was a passenger in the car. This was further modified to provide commercial property coverage as part of the excess line. Only recently, when required by California law, did the TNCs agree to provide the commercial insurance when providing ride-sharing services with a reduced level of coverage while in search mode (app on) and with a higher level of coverage while actively connected to or transporting a passenger. See regulatory development in the following section.

seven passengers). The PAP excludes coverage when driving for hire. In an attempt to avoid higher premiums, some drivers may not report their business activities to insurers. This type of misrepresentation could give the insurer the right to cancel the policy or refuse to pay a claim.

Physical Damage to Owners Vehicles

The above noted exclusions applying to liability also apply to physical damage in the PAPs. Additionally, homeowners policies will typically state that motor vehicles are not covered property.

Other Insurance

The typical homeowners policy issued on an Insurance Services Office, Inc. (ISO) form excludes motor vehicle liability, personal liability, and medical payments arising out of or in connection with a business. ISO homeowners forms also excludes sexual molestation, corporal punishment, or physical or mental abuse. A personal umbrella policy (PUP), if purchased, can provide additional limits, usually from \$1 million to \$5 million of liability above coverage provided under the PAP and HO. An umbrella policy will, under certain circumstances, provide broader coverage and “drop down” if coverage is unavailable on the PAP or the HO policy. However, the PUP has exclusion for damages arising out of business or professional pursuits, and most contain auto liability follow form conditions, such that if not covered in the auto policy, the umbrella would not provide any coverage.

Exposure Issues for Insurance Providers

Insurers Providing Personal Automobile Policies to Ride-sharing Drivers

While insurance contracts are clear regarding the lack of coverage for commercial uses of an automobile (livery exclusion), it is not clear whether coverage can be denied when the automobile is being used for noncommercial activities (i.e., when the app is not being used). Risks may increase in tandem with increased mileage, lack of vehicle maintenance, and long hours on the road or in unfamiliar locations. It is critical that insurers are clear regarding whether they will provide this coverage and in asking applicants and renewal customers if they

are providing ride-sharing services. In the event that a lawsuit is filed and coverage is confirmed to exist, ISO's PAP and commercial auto policy (CAP) provide defense **in addition to** the policy limits. The duty to defend or settle ends when the liability coverage limit of insurance has been exhausted by payment of judgments or settlements. There is no duty to defend any suit or settle any claims for bodily injury or property damage not covered by the policies, but the insurer may end up covering losses and defending suits that should be covered under the TNC commercial policy.

An important issue for the insurance industry may be the development and pricing of hybrid policies. The California legislation discussed in the next section requires the TNCs to provide a commercial automotive policy as primary protection, but allows this to be replaced by individual (hybrid) insurance policies that provide commercial protection. This is a Big Data issue that requires analysis of the risks of the heterogeneous ride-sharing population. Actuaries and underwriters will need to have data regarding individual driving habits—where, when, and for how many hours a day a driver is involved in ride-sharing activities versus personal use and not just where the car is garaged and how many miles are reported to be driven. They will require data from the TNCs to develop and price policies and to present these policies to regulatory authorities as required.

Insurance agents and brokers

Insurance agents have a greater exposure to E&O claims for failure to identify, disclose, and address the exposures and potential gaps in coverage. The agent must review all pertinent documentation, gain an understanding of the regulatory requirements, and communicate the risks with underwriters before presenting options to a client.

Regulations—A Moving Target

In 2013, the California Public Utility Commission (CPUC) undertook an analysis of the ride-sharing industry, which the CPUC termed Transportation Network Companies (to distinguish TNCs from traditional providers of taxi services). The reaction was initially negative. The CPUC conducted extensive hearings and received wide-reaching comments. In **DECISION 13-09-045**, dated Sept 19, 2013, the Public Utilities Commission of the State of California granted

TNCs the right to continue operating while a more comprehensive evaluation took place. The commission concluded that these companies were transportation providers, not technology companies, and labeled them Transportation Network Companies, or TNCs. The action established that the CPUC had authority to regulate the ride-share companies. Immediately after these hearings, the TNCs received cease-and-desist letters and fines.¹⁴

Since the date this report was issued, the CPUC has had a number of hearings and received a considerable amount of written comments from supporters of the report and opponents to ride sharing. Among these was a report and testimony from the California Department of Insurance Commissioner.¹⁵

California Insurance Commissioner Dave Jones held an informational hearing on TNC insurance on March 21, 2014. Following this hearing, Commissioner Jones concluded there were far too many “gaps” in insurance protection. In a letter dated April 7, 2014, to President Peevey of the CPUC, Jones outlined these gaps and provided recommendations.

In summary, the TNCs were required to provide coverage to fill in these gaps during three distinct periods:

- Period 1: App Open → No match
- Period 2: Match accepted → Passenger pickup
- Period 3: Passenger in Car → Passenger has safely exited the vehicle.

The TNCs are required to file evidence of \$1,000,000 commercial liability insurance, \$50,000 comprehensive collision coverage, and \$1,000,000 uninsured and underinsured motorists coverage for each driver. The insurance must be “exclusive” and “assume all liability,” including the “sole duty to defend.” In addition, the CPUC requires the TNC to perform driver screening—including criminal background checks, motor vehicle records, nineteen-point vehicle

¹⁴Don Wise, “Notice to Cease and Desist,” California Public Utilities Commission, Case PSG-3360, August 15, 2012, www.cpuc.ca.gov/NR/rdonlyres/03851232-DD84-47C1-B134-D90C8D15D3B7/0/CeaseandDesistLetters.pdf (accessed November 25, 2014).

¹⁵ Dave Jones, Letter to California Public Utilities Commission Michael R. Peevey, California Department of Insurance, April 7, 2014, www.insurance.ca.gov/0400-news/multimedia/0030VideoHearings/upload/CDI-CPUC20140407.pdf (accessed November 25, 2014).

inspections—and to maintain records that would be subject to audit. It was recommended that the requirements be delayed sixty days to enable the TNCs to secure additional coverages.

Based on Commissioner Jones' recommendations and input from the TNCs and other concerned parties, on June 10, 2014, the Public Utilities Commission filed a ***PROPOSED MODIFICATION TO DECISION 13-09-045***, which adopted rules and regulations for TNCs.¹⁶ The ruling requires TNCs to file evidence of insurance with the CPUC as part of the permit application and renewal process. Although the policy will extend coverage, it is the driver's responsibility to have knowledge of the regulations. As in the commissioner's recommendations, the ruling does not discuss Period "0" (when the driver is not using the app and is instead driving for personal needs) and whether primary insurers would be expected to provide coverage during this period. This uncertainty underlies a significant gap for part-time drivers.

While regulation has advanced significantly in California, there are regulatory issues that still need to be addressed. Insurance regulators may need to approve modifications or endorsements (and changes in pricing) for PAPs that allow coverage for ride sharing or the approval of commercial policies that mimic personal policies, but allow for livery options. This may extend to personal umbrella policies. The pricing of such policies may be based on mileage driven and the time and location of the ride-sharing vehicle (during all three periods), not just where the car is garaged. All of these will require analysis of data-comprehensive sharing of information between the TNCs and insurers (as well as regulators).

Legislative Process

On September 2, 2014, the California legislature passed an amended version of Assembly Bill 2293 (Bolina) that establishes guidelines for TNC insurance coverage. It passed the assembly by

¹⁶ Public Utilities Commission, State of California, "Decision Adopting Rules and Regulations to Protect Public Safety While Allowing New Entrants to the Transportation Industry," Decision 13-09-045, September 23, 2013, <http://docs.cpuc.ca.gov/PublishedDocs/Published/G000/M077/K192/77192335.pdf> (accessed November 25, 2014).

30-4 (6 no-vote recorded) and the Senate by 73-0 (6 no-vote recorded). Governor Brown signed this bill into law on September 17, 2014. The legislation does the following¹⁷:

- Codifies the CPUC definition of TNC.
- Requires TNCs to inform drivers about insurance coverage and limits offered by the TNC when providing TNC services and that a driver's personal auto coverage may not provide coverage when operating as a TNC.
- Defines when personal and commercial auto insurance is in effect.
- Adopts the three periods specified by the CPUC. Key provisions in this bill would require a TNC or TNC driver, as of July 1, 2015, to maintain primary liability insurance coverage at the following levels:
 - From the moment a participating driver accepts a ride request until the driver completes the transaction or until the ride is complete: Primary insurance of \$1 million for death, personal injury, and property damage.
 - TNC insurance shall also provide \$1 million uninsured and underinsured motorists coverage from the moment a passenger enters a participating driver's vehicle until the passenger exits the vehicle.
 - From the moment a participating driver logs on to the application until the driver accepts a request: Primary insurance of \$50,000 for death and personal injury per person, \$100,000 for death and personal injury per incident, and \$30,000 for property damage. At least \$200,000 of excess liability insurance must be maintained by the TNC during this time.
- Flexibility in the type of insurance policy is provided by allowing the driver to purchase a smaller policy for the period before a ride match is accepted, accompanied by a TNC purchased excess policy, bringing coverage to the \$100,000/\$300,000/\$50,000 level.
- Nothing in the bill restricts the PUC from determining that higher limits are appropriate.
- The bill requires a TNC or its insurer to cooperate with insurers that are involved in the claims coverage investigation for the exchange of information, including the times that a driver logged on and off of the online-enabled application or platform.
- There is a requirement for the California Department of Insurance and the CPUC to study TNC insurance rates and report to the legislature by December 31, 2017.

AB2293 makes it clear that a driver's personal insurance will have no duty to defend or indemnify TNC accidents unless that insurance has been "specifically written to cover the

¹⁷ California Legislative Information, AB-2293, Transportation network companies: insurance coverage, September 17, 2014, http://leginfo.ca.gov/faces/billNavClient.xhtml?bill_id=201320140AB2293 (accessed November 25, 2014).

driver's use of a vehicle in connection with a transportation network company's online-enabled application or platform."¹⁸

As a method to entice the insurance industry to develop new, hybrid products, these organizations should develop and implement risk management best practices with CPUC regulatory compliance as a minimum standard (CPUC, 2013).

¹⁸ Brooks, "California Bill Would Enable Uber, Lyft Drivers to Finally Get Insurance.

Short-Term Rentals in a sharing economy

“For Rent: Charming room with private bath in converted attic with balcony overlooking downtown—\$125 per night including parking” (www.airbnb.com). A similar ad at a train station or city center in 1860 may have read: “Board only. One dollar per day, reasonable per week. Contact: Ms. Smith.”

History:

Today’s phenomenon of short-term rentals is not new, but the use of short-term rental websites such as airbnb.com, vrbo.com, homeexchange.com, and others ("STRs") certainly is changing the way people seek out lodging today. Boarding homes and rented rooms were a key part of how 19th-century cities grew; historians estimate that between one-third and one-half of 19th-century urban residents were either boarders themselves, or people who took boarders into their homes.¹⁹ The 1920s saw the emergence of zoning laws that significantly impacted where and how boarding houses and residential hotels operated.²⁰

As time passed, so did the technology for connecting socially and for advertising. Today, through online SNCs, a traveler can book a furnished rental in many cities with a click of the mouse, providing a more local experience than most hotels can.

¹⁹ Ruth Graham, “Boardinghouses: Where the City Was Born,” *The Boston Globe*, January 13, 2013, www.bostonglobe.com/ideas/2013/01/13/boardinghouses-where-city-was-born/Hpstvt0kj52ZMpjUOM5RJ/story.html (accessed November 25, 2014).

²⁰ Alan Durning, “Rooming Houses: History’s Affordable Quarters,” *Sightline Daily*, November 14, 2012, <http://daily.sightline.org/2012/11/14/rooming-houses-historys-affordable-quarters/> (accessed November 25, 2014).

Key Short-Term Rental STRs

Airbnb, headquartered in San Francisco, was founded in August 2008; its current market valuation is estimated to be approximately \$10 billion.²³ Airbnb will (by the end of 2014) require that all hosts have working smoke and carbon monoxide detectors installed in listed properties.²⁴ It provides a list of suggested actions for hosts who wish to make their listed properties safer for guests (including having clearly marked fire escape routes, removing trip-and-fall hazards, child-proofing, etc.)²⁵; however, there is no apparent mechanism for verification or enforcement of any of the suggested safety/risk reduction items. Airbnb does provide hosts with a \$1 million “Host Guarantee” that protects the host’s covered property from property damage caused by guests.²⁶ Starting on January 15, 2015, Airbnb will also provide a \$1 million liability insurance policy that protects hosts (as well as landlords and Homeowners Associations) from claims related to the renting of their properties through Airbnb.²⁷

With regard to local regulations that may apply to a

Major Short Term Rental Companies

Airbnb

Cities: 33,000

Countries: 192

Venture Financing: \$826 million

VRBO

Listing: >1 million worldwide

Countries: 190

Publicly Traded: NASDAQ: AWAY

HomeExchange

Listing: 55,000 ‘listings’ and over 1 million ‘exchanges’ worldwide

Countries: 150

Venture Financing: Unknown

²³ Ingrid Lunden, “Airbnb Has Closed Its \$500M Round of Funding at a \$10B Valuation, Led by TPG,” TechCrunch, April 18, 2014, <http://techcrunch.com/2014/04/18/airbnb-has-closed-its-500m-round-of-funding-at-a-10b-valuation-led-by-tpg/> (accessed November 25, 2014).

²⁴ Airbnb, Help Center, “I’m a Host. Am I Required to Have a Smoke and CO Detector Installed?,” <https://www.airbnb.com/help/article/515> (accessed November 25, 2014).

²⁵ Airbnb, Help Center, “What Can I Do to Make My Space Safer for Guests?,” <https://www.airbnb.com/help/article/509> (accessed November 25, 2014).

²⁶ Airbnb, Help Center, “What is the Airbnb Host Guarantee?,” <https://www.airbnb.com/help/article/279> (accessed December 10, 2014)

²⁷ Airbnb, Help Center, Trust and Safety, Home Safety, <https://www.airbnb.com/host-protection-insurance> (accessed December 10, 2014)

host's rental activities, the Airbnb website states that there may be laws or regulations that restrict or prohibit rental of one's property on a short-term basis; however, it is the responsibility of the host to determine all applicable laws and to comply therewith.²⁸

VRBO²⁹ (Vacation Rentals by Owner) is an online vacation-rental marketplace founded in 1995 by a couple who wanted to facilitate rental of their ski condo in Colorado.³⁰ VRBO was acquired by HomeAway in 2006 in a transaction valued at \$160 million.³¹

The terms and conditions of the VRBO user agreement³² state that the company is not a party to the rental transaction; does not provide liability insurance for owners, property managers, or travelers; and charges owners with responsibility for complying with applicable taxes, permit or license requirements, zoning ordinances, safety, and antidiscrimination and fair housing laws.

HomeExchange.com provides a service whereby individuals can trade their residence with another individual for a period of time. The company's website³³ states that more than 55,000 homes in more than 150 countries are available. While a membership fee is required to sign up on HomeExchange, no money is paid between the parties that trade residences.

Individual Parties Involved With Shared Rentals

Owners of properties who rent their home are likely considered "unincorporated vendors" used by the STR.³⁴ Owners receive IRS 1099 forms for the income produced by their rental-sharing activities. Owners are responsible for personal and/or self-employment taxes, Social Security and Medicare taxes, and generally any local and occupancy taxes that apply.

²⁸ Airbnb, Help Center, "What Legal and Regulatory Issues Should I Consider Before Hosting on Airbnb?," <https://www.airbnb.com/help/article/376> (accessed November 25, 2014).

²⁹ Wikipedia, "VRBO," <http://en.wikipedia.org/wiki/VRBO> (accessed November 25, 2014).

³⁰ InterviewBooks.com, Net Success Interviews: VRBO, www.interviewbooks.com/vrbo_com.htm.

³¹ http://www.homeaway.com/info/media-center/press-releases/PR_2006/VRBO_1 (accessed November 25, 2014).

³² VRBO, Terms and Conditions, August 28, 2014, www.vrbo.com/global/termsandconditions.htm (accessed November 25, 2014).

³³ HomeExchange.com, <https://www.homeexchange.com/en/registration/membership-options/> (accessed November 25, 2014).

³⁴ NFIB Research Foundation, Crib Sheet 12-5, June 22, 2012, www.nfib.com/Portals/0/PDF/AllUsers/research/cribsheets/1099-requirements-nfib-cribsheet.pdf (accessed November 25, 2014).

Most existing housing and hotel regulations distinguish between a lodger, a tenant, a boarder, and a guest. According to the American Heritage Dictionary, a lodger is defined as one who rents and lives in a furnished room in a house where the owner lives. A tenant is defined as one who temporarily lives in a property owned by another. A boarder is defined as one who pays for both meals and lodging at another's home. Lodgers, tenants, and boarders typically live in a property for more than thirty days. A **guest** is defined as one who lives in another's property for less than thirty days. ***A guest who pays for the accommodation is how we are defining a short-term or casual renter and is the subject of this paper.***

Controversies

Short-term renters have traditionally had many options, ranging from hotels, motels, inns, bed and breakfasts to YMCAs. There are many regulations that the owners and operators of those establishments must follow, depending upon the jurisdiction in which they are located. These include life and safety rules, food and beverage licenses and standards, and various taxes that must be collected. The sharing economy has provided the short-term renter with a new option—using host websites like Airbnb, VRBO, HomeExchange—and the debate from all sides is in full swing.

The main debate is primarily focused on the use of multidwelling buildings (apartments, condominiums and tenancies in common) and the rapid rise of Internet-based rentals on a short-term basis. Rentals of any length of *single-family* homes have generally not been the subject of regulation or the recent short-term rental controversy (with the notable exceptions of San Francisco and New York City), although individual applicable housing association rules may govern the rental practice.

The topic is proving to be a political wedge in large cities, with San Francisco, New York, and Chicago leading the charge addressing the issues. Angry neighbors, consumer advocates,

THE 'ACCIDENTAL' TENANT

A renter of a Palm Springs, California, condominium that was rented through Airbnb refused to vacate after his 44-day rental that started in June 2014, claiming California tenancy rights, having rented for more than 30 days. However, he voluntarily vacated the property in August 2014.

and housing-equality supporters have voiced objections against STRs and individuals who rent out their properties (who are often just looking to supplement their income or cover their mortgage). Of particular note is the argument made by hotel owners associations and unions about the lack of hotel taxes being collected.

Airbnb states that its hosts are responsible for following all laws and regulations, including paying any local taxes that apply to their accommodations. Airbnb facilitates the collection and remittance of occupancy-related taxes on behalf of hosts in certain areas. As a U.S.-based company, Airbnb is also required by U.S. law to collect taxpayer information from hosts who appear to have U.S.-sourced income. It is the host's responsibility to report the proper taxable income on their U.S. and state income tax returns.³⁸

Owners also have to understand when a guest might become a tenant and therefore be protected under various tenant regulations. A casual weekend renter may just turn out to be an unintended long-term tenant.^{39 40} (See Sidebar on page 22)

Risk Exposures:

As of this writing, there are no publicly known significant settlements or jury awards involving short-term rentals, although incidents where guests overstay their arranged rental period and subsequently demand permanent renter protections have increasingly made news headlines. The following examines key exposures present for the parties involved with these shared rental transactions.

Liability for STRs:

³⁸ www.Airbnb.com

³⁹ Carolyn Said, "Squatters Don't Sit Well With Airbnb Tests," *San Francisco Chronicle*, July 25, 2014, www.sfgate.com/business/article/Squatters-don-t-sit-well-with-Airbnb-hosts-5631952.php (accessed November 25, 2014).

⁴⁰ Skip Descant, "Airbnb Squatter Checks Out of Palm Springs Apartment," *The Desert Sun*, August 20, 2014, www.desertsun.com/story/money/business/tourism/2014/08/20/airbnb-palm-springs-squatter/14362779/ (accessed November 25, 2014).

Liabilities extend beyond the typical business liability. As a web- and app-based business, the cyber liability exposure is real, with payment card, banking account, and other personally identifying information collected and stored about renters and guests. Liability for notification and credit-repair expenses arising from a data breach are a reality, as was seen in the Target stores data breach of 2013.⁴¹

Libel and defamation potential exists anytime individuals can express their opinions publically. Guests and owners alike can review their rental experience publicly on the STR's websites. While this potentially exposes these individuals to libel or defamation risks, the STR is likely shielded from responsibility by the Communications Decency Act (47 U.S.C 230), which protects it from a range of laws that might otherwise be used to hold the STR legally responsible for what others say and do.⁴² In an interesting twist, a 2014 working paper published by Harvard Business School empirically investigated the extent of racial discrimination *against hosts*, rather than against guests, on Airbnb.⁴³

Such nuances suggest an emerging legal environment that may have implications for the general and management liability exposures for these STRs that were, perhaps, not envisioned when they started.

Property Damage Exposures for Owners:

As with any furnished rental, an owner runs the risk of a guest damaging or stealing personal property from the unit.

Liability Exposures for Owners:

⁴¹Judy Greenwald, "Target Maxes Out Insurance Coverage for 2013 Data Breach," *Business Insurance*, August 6, 2014, www.businessinsurance.com/article/20140806/NEWS07/140809889/1246 (accessed November 25, 2014).

⁴²47 U.S. Code §230 – Protection for private blocking and screening of offensive material, <http://www.law.cornell.edu/uscode/text/47/230> (accessed December 10, 2014)

⁴³ Benjamin Edelman and Michael Luca, "Digital Discrimination: The Case of Airbnb.com," (working paper 14-054, Harvard Business School, January 10, 2014), www.hbs.edu/faculty/Publication%20Files/14-054_e3c04a43-c0cf-4ed8-91bf-cb0ea4ba59c6.pdf (accessed November 25, 2014).

A third-party duty of care is imposed upon the owners of rental properties, from simple slip-and-fall incidents to catastrophic scenarios involving a death on the property. The more amenities or features a property offers, the more the potential exposures increase. Owners should consider the controls in place for general security and to mitigate loss from common and not-so-common exposures, including:

- Proper egress—Short-term rentals can exist in basements and attics, where egress may be limited, as these spaces were not designed for regular residential use, per se.
- Swimming pools and spas—Owners should ensure that these areas are properly fenced to prevent access by children and that the necessary safety equipment is available in the event of an emergency.
- Leisure and recreation—Saunas, fitness equipment, trampolines, bicycles, and other sports and leisure options increase the duty of care required of the owner of the property. While these make the property more attractive for guests, they also increase the liability exposure to the owner and should be controlled as best as possible. Vacation rentals on bodies of water pose potential additional exposures if swimming is permitted or watercraft is available.
- Premises security—For rental units in secured properties such as high-rise condominiums, allowing a short-term guest onto the premise increases the liability of the lessor to others within the building. Consider the potential liability to an owner whose short-term guest is responsible for property damage or bodily injury to others within the building.
- Disability access and discrimination—Generally, places of public accommodation located in private residences have an exemption from compliance with the Americans with Disabilities Act (ADA) Title III regulations if *they are owner-occupied establishments renting fewer than six rooms*.⁴⁴ Federal and local regulations and definitions associated

⁴⁴ § 36.207 [Americans with Disabilities Act Title III Regulations], www.ada.gov/regs2010/titleIII_2010/titleIII_2010_regulations.htm#a207 (accessed November 25, 2014).

with this emerging trend are unsettled, and the residence may not be owner occupied in the case of vacation home or entire apartment/home rentals. The applicability of ADA Title III and potential discrimination exposure is one that will need to be watched closely. Furthermore, because owners generally have the right to reject a rental request,⁴⁵ there is an inherent potential for a rejection to be construed as biased or unfair by the guest. General liability and homeowners policies may explicitly exclude coverage for discrimination, leaving the owner potentially responsible for defense and indemnity.

Owners should balance exposures presented by the short-term rental of their properties, their assets, and the amount of insurance purchased for such exposures. Umbrella or excess liability insurance is a likely sound choice for lessors of any property.

Liability Issues for Related Third Parties

Other parties may have increased liability from the sharing economy. Consider the following:

For condominiums, TICs, and other shared-ownership structures, the homeowners association may also be exposed to vicarious liability, particularly if a rental restriction exists in the association governing documents that was not enforced by the board or management company or if a guest is using a common area or amenity.

The issues of liability are potentially complicated by regulations or restrictions that apply to the use of the property in question. Zoning restrictions or ordinances often govern the legality of short-term rentals, whether a single room in a home or the entire home itself. Violation of law could result in a strict liability approach to a claim or suit.

Insurance agents would be wise to counsel customers on the potential coverage gaps in their personal insurance policies for these business pursuits. In addition, insurance carriers must clearly communicate to their agents and policyholders any changes in insurance contract language that may impact the availability of coverage.

⁴⁵ Airbnb, Help Center, "Am I Allowed to Decline Reservation Requests?," <https://www.airbnb.com/help/article/360> (accessed November 25, 2014).

Other Issues for Related Third Parties

The owner of a condominium or similar shared-ownership structure faces a more complex situation than a single homeowner renting a vacation home via vrbo.com, for example. The Covenants, Conditions & Restrictions (CC&Rs) regulating permitted use of the unit or home will likely contain a minimum rental contract-period requirement, if they allow rentals at all. In addition to the liability issues explored above, there are other financial implications to increased rentals in condominiums, apartments, and TICs. Underwriters insuring these properties assume relatively stable exposures throughout the policy term. Short-term rentals introduce volatility that may affect the availability of both property and liability insurance. Further, as rental units increase within a multidwelling structure or complex, availability of home loans afforded to new buyers within the association may be impacted, particularly with FHA-backed loans that limit percentages of rental units within the complex.

Insurance Issues

Unlike the TNC's support of the shared transportation service sector, the STR's support of short-term rentals does not verify the existence or adequacy of insurance of either party.

Individuals should be aware that liability arising out of renting their residence to a third party may or may not be covered under their homeowners or renters insurance policies, by virtue of a business pursuits exclusion or similarly worded exclusion, or by other policy language.

For the purposes of this discussion, the policy wording of the ISO HO-02 (Homeowners—Broad Form), ISO HO-03 (Homeowners—Special Form [i.e., Named Peril]), and ISO HO-06 (Unit-Owners Form) were examined. The wording of the HO-02, HO-03, and HO-06 are identical or substantially similar in the following areas:

Property—With regard to property coverages, the personal property of roomers, boarders, or other tenants is excluded from coverage.

Liability—With regard to liability coverages, the aforementioned ISO policies could be read to exclude coverage for renting one's residence in some instances. The policies exclude "business" activities, which are defined as activities for which an insured receives more than

\$2,000 in compensation during the twelve months preceding the policy period. The exclusion does not apply to rental of an insured location on an occasional basis; however, “occasional” is not defined within the policies.

When a short-term rental includes use of the host’s automobile or watercraft, motor vehicle liability and watercraft liability are excluded if the vehicle or watercraft is being rented to others or is used for any business purpose.

Proprietary company homeowners/condominium policy forms may allow some sort of occasional rentals (although, again, “occasional” may not be defined) or rentals “in part” (e.g., rental of a room within a dwelling when the insured also occupies the dwelling).

In light of the foregoing, individuals should carefully examine their insurance policies prior to engaging in a short-term rental of their property and may wish to investigate securing coverage either by adding an endorsement to their homeowners policy or purchasing a separate rental home policy or condominium rental policy. A common method of accomplishing this would be to purchase a policy based on ISO form HO-1733 (Unit-Owners Rental to Others). HO-1733 attaches to and modifies several clauses within the HO-06 (Unit-Owners Form), thereby granting coverage for property that is rented to others. An umbrella liability policy may provide additional coverage.

Regulations—A Moving Target:

The industry is just beginning to address the debates through regulation and legislation. With the controversies brewing as earlier mentioned, it is no surprise that regulation meant to protect the stakeholders is already on the table.

San Francisco has five different sections of laws that many owners probably violate, ranging from zoning restrictions to rent control and tax laws.⁴⁷ The San Francisco District Attorney has filed a pair of lawsuits against local landlords who illegally rent apartments on a

⁴⁷ Steven T. Jones and Parker Yesko, “Into Thin Air,” *San Francisco Bay Guardian*, August 6, 2013, www.sfbg.com/2013/08/06/thin-air (accessed November 25, 2014).

short-term basis. The San Francisco Apartment Conversion Ordinance prescribes penalties of \$1,000 per day for buildings with four or more units renting out units for less than thirty days.⁴⁸

In the October, 2014, the San Francisco Board of Supervisors passed a law (to become effective in February, 2015) that places some limits on short-term rentals.⁵² The law allows only permanent residents to offer short-term rentals, establishes a new city registry for hosts, mandates the collection of hotel tax, limits entire-home rentals to 90 days per year, requires each listing to carry \$500,000 in liability insurance, and establishes guidelines for enforcement by the planning department.

In New York, reports of fines as high as \$40,000 for violating its laws⁵³ on short-term rentals have been reported.⁵⁴ The state lost a bid to subpoena information from Airbnb about guests using Airbnb's website to advertise short-term apartment rentals in New York City. A New York State law prohibits owners or renters of apartments in multiunit buildings from renting units for less than thirty days unless they remain present. The law permits having boarders or lodgers. Airbnb, despite winning the subpoena lawsuit, has now agreed to provide the information to the New York attorney general and to identify the name or tax identification of the hosts within the following year.⁵⁵

Short-Term Rentals—Conclusions:

While short-term rentals are not a new phenomenon, the risk management implications of the emerging sharing economy can be complicated and perhaps not fully addressed through the insurance mechanism. There is an opportunity to educate owners about their legal

⁴⁸ Steven T. Jones, "Lawsuits Go After SF Landlords Doing Illegal Short-Term Apartment Rentals," San Francisco Bay Guardian, April 23, 2014, www.sfbg.com/politics/2014/04/23/lawsuits-go-after-sf-landlords-doing-illegal-short-term-apartment-rentals (accessed November 25, 2014).

⁵² <http://www.sfgate.com/news/article/Supervisors-approve-Airbnb-law-5807858.php> (accessed December 10, 2014)

⁵³ Laws of New York (2010), Chapter 225, www.nyc.gov/html/dob/downloads/pdf/NYS_chapter_225.pdf (accessed November 25, 2014).

⁵⁴ Ron Lieber, "A Warning for Hosts of Airbnb Travelers," The New York Times, November 30, 2012, www.nytimes.com/2012/12/01/your-money/a-warning-for-airbnb-hosts-who-may-be-breaking-the-law.html (accessed November 25, 2014).

⁵⁵ "Airbnb Agrees to Disclose Some Data," *San Francisco Chronicle*, May 22, 2014, p. C5.

responsibilities as short-term landlords and about their need for appropriate and adequate insurance. Further, there are opportunities for insurers to enhance or make more readily available insurance products tailored for these exposures. The sharing economy' is resonating with consumers and provides an opportunity for enterprising new thoughts on risk management.

Summary and Recommendations

The sharing economy, at its core, is largely an attempt to aid individuals with underutilized assets to extract value from these assets by connecting with individuals who are willing to pay for using the shared assets. This sharing is facilitated through the development of high-tech platforms that, for a fee, expedite connections and reduce information asymmetries. As the sharing markets continue to change, regulatory and tax structures will need to adapt to these changes, as will insurance markets, insurance institutions, and insurance policies.

Ride sharing is considered by the insurance industry to be a commercial activity; the standard ISO PAP excludes commercial use in general and livery services in particular. This can leave drivers in insurance/legal limbo. California has recently addressed the insurance issues by requiring the TNCs to maintain and file proof of primary insurance with the CPUC. We anticipate that other states may follow California's lead.

Short-term rentals can also result in gaps between expected and actual insurance coverage. This is because of limitations in coverage for commercial activities in standard ISO homeowner policies when renting a location on an occasional basis or renting in part when the owner also occupies the dwelling (and when more than \$2,000 in annual revenues is generated). Additionally, insurance coverage is not afforded for activities that are prohibited by law. Several large cities are considering or have passed regulations and/or legislation prohibiting some types of home sharing. In these situations, there may be no insurance coverage.

The insurance industry needs to take action in several areas, as risks associated with the sharing economy expand and change risk patterns from those typically observed in historical loss statistics used for rate making and underwriting decisions. Four of these are considered priority.

First, it is incumbent on the insurance industry, insurance experts, and academics to be actively involved in insurance and risk management discussions with sharing economy firms, public utility and insurance regulators, and the public. It must be made clear where insurance coverage exists and where specific activities are excluded. Each insurer must determine its risk

appetite, verify risk exposures through the application process, and diligently underwrite and price coverage according to the exposures. As an example, an insurer must determine whether it will provide personal auto insurance to individuals engaging in ride-sharing services while only using their car for personal reasons or whether all ride-share activities will result in the cancellation of insurance coverage. An insurer must also determine whether its homeowner policies will cover the liability exposures for paying guests when the activity is more than occasional. It goes without saying that decisions regarding the acceptance of sharing economy services must be disseminated throughout the firm and to brokers or independent agents that communicate with the insurance buyers.

Second, there is undoubtedly a role for the insurance industry in the development of hybrid policies that amend existing personal auto and homeowners policies to include coverage for commercial activities involving ride sharing and home sharing (as well as other sharing economy activities). Alternatively, the insurance industry could provide commercial policies that include the coverage expected in standard personal policies. The California legislation that requires TNCs to provide primary protection does allow drivers to carry commercial coverage as primary, with the TNC coverage as excess. There will undoubtedly be efforts by the TNC to encourage the development of such policies. Properly structured and priced policies are a potential for profitable expansion for innovative insurers. Sharing of information between the TNC and the insurer regarding the usage (hours driven with an app on, with the app connected to a rider or with a rider in the car, and with the app turned off) can be critical in addressing the heterogeneity of the ride-share driver population. Likewise, the number of rental days can be communicated for vacation homes, rooms, or complete residences (and whether the use of an automobile is included in the transaction) in establishing appropriate insurance rates and coverage for liability for injury to a paying guest. In both cases, insurers will need access to information from multiple sharing companies as drivers, or property owners may use multiple sharing services. A proper exploitation of this data-rich environment will allow a clearer understanding of the risks and ensure fair and competitive pricing.

Third, the direct risks associated with automobile or property insurance reflect only a portion of the risks faced by individuals operating in the sharing economy. Participants are

generally considered independent contractors by the ride-sharing companies and may be sole proprietors in home sharing. As such, they will often be without coverage for workers compensation, short and long-term disabilities, or medical costs not directly related to an accident. In some jurisdictions, liability insurance provided by the TNCs may be considered insufficient, and drivers may wish to purchase an umbrella policy to increase the level of protection. Likewise, the provision of primary insurance by the TNC may not be sufficient to cover the TNC's liability, and a form of stop loss reinsurance may be required. The insurance industry should be able to develop products that provide optional coverage for these types of risks.

Finally, this task force considers it essential that participants involved in the sharing economy undertake risk management practices that will protect not just the participants, but also the nonparticipating public. Inaccurate claims regarding the legality of services and/or of liability or property coverage by personal insurance policies as primary coverage are disservices to the markets they are trying to build. The sharing economy firms may be creating liabilities for themselves by not directly and openly addressing insurance coverage and exclusions.

Disinformation has been more a problem from ride-sharing services than home sharing services. Home-sharing services have largely avoided the problem by stating that the property owners are responsible for ensuring the legality of operations and insurance coverage, but there are undoubtedly liabilities lurking below the surface. Coordination and cooperation with the insurance industry and insurance and academic experts in developing coverage options and following prudential risk management practices should be high-level priorities for those who are expanding existing or contemplating future opportunities within the sharing economy.

The sharing economy has presented us with an excellent example of how new risk exposures emerge and change as time progresses. Courts, regulators and legislators have been forced to deal with these changes, although the outcome is sometimes inconsistent. This creates even greater challenges to the risk management and insurance industry. As insurance professionals, we acknowledge that such changes are constant and we must strive to work together to provide solutions.



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