Executive Summary

The newly created sharing economy has revolutionized the way individuals utilize resources. Since its founding in 2008, Airbnb, a web-based service that connects travelers and hosts, has given individuals the opportunity to rent out their homes on a short-term basis. Despite its rapid growth and wide appeal, Airbnb’s unique business model has raised challenging questions on how to regulate the home-sharing industry. This paper focuses on two important issues – the effect of Airbnb’s short-term rentals on housing supply and the safety and insurance ramifications of Airbnb’s operations – and proposes practical regulatory solutions that adequately address these considerations without compromising Airbnb’s innovative and unique business model.

In the forthcoming case study, we begin by introducing the sharing economy, outlining its history, its basic elements, and its major players. We then introduce Airbnb, its history, its business model, and its key competitors. Next, we discuss the challenges in regulating the sharing economy, providing some legal and historical context. We go on to describe the long regulatory battle between Airbnb and New York State officials. These regulatory proceedings largely inform our ultimate conclusions and policy recommendations. Moving on to our recommendations, we first outline the key stakeholders involved in Airbnb’s business model. Finally, we explore two important issues in need of a more comprehensive regulatory scheme and propose policies to address the risk they pose, while preserving the benefits Airbnb delivers.
Introduction to the Sharing Economy

The sharing economy is a system built around the sharing of human and physical resources. It is made up of web-based peer-to-peer marketplaces. And the internet, further revolutionized the sharing economy. Communities have shared assets for thousands of years, but the full extent of the sharing economy did not surface until the age of the Internet. The Internet reduced transaction costs, which allow for facilitated transmission of information between parties. According to research compiled from professors at Princeton University, University of California, Berkeley, the sharing economy has created people with more opportunities to earn money in addition to a full-time or part-time job. As of 2015, 44 percent of US consumers were familiar with the sharing economy and 19 percent of the total US adult population engaged in a sharing economy transaction. The breakdown of the percentage is shown in Figure 1.


The Internet coupled with new technology and operations defines the sharing economy, however, the sharing economy also stands on core pillars. The core pillars of the sharing economy illustrate its benefits. These pillars include: digital platforms connecting capacity and demand; transactions offering access over ownership; collaborative forms of consumption; branded experiences driving emotional connection; and understanding an economy built on trust. While some of the pillars are not unique to the sharing economy, the pillars allow for the sharing of more assets. First, platforms that connect capacity and demand by hosting sharing economy business models. Digital platforms measure available market capacity and connect that capacity with those who need it. For example, Airbnb matches spare rooms and apartments with travelers in need of lodging. Second, transactions offer access instead of ownership. The access includes renting, lending, subscribing, reselling, swapping, and donating. Third, collaborative forms of consumption. These transactions involve deeper forms of social interactions. For example, Airbnb and Couchsurfing provide travelers with the ability to connect with hosts and

Figure 1
receive personalized travel tips. For lower prices, one can get similar services from luxury hotels without the high cost of personalization inherent in the traditional economy. Fourth, branded experiences drive emotional connection to the middleman. Companies need to manage links and social connections for successful marketing. Fifth, the economy is built on trust and understanding. About one-fifth of American consumers participate in the sharing economy. In general, 64% of consumers believe government regulation is less important than peer regulation in the sharing economy. The combination of digital platforms connecting capacity and demand; transactions offering access over ownership; collaborative forms of consumption; branded experiences driving emotional connection; and understanding an economy built on trust differentiate the sharing economy from the nondescript trading and bartering that eventually morphed into today’s sharing economy. These pillars create a strong basis for the sharing economy to exist and grow. Because the sharing economy holds the basis of each of these pillars, it significantly impacts local, national, and international economies as well.

The sharing economy has emerged as an additional supplier of goods and services to those already on the market. As the size of the sharing economy grows, so does the magnitude of its economic impacts. Already established businesses are forced to enter the sharing economy in some way to keep up with the society. The sharing economy supplies the outlet for established companies to recognize and support their customers’ desire to resell products. This part of the sharing economy describes e-bay or amazon marketplace, however, Airbnb and Uber, for example, deal with a more evolved sharing economy. Airbnb and Uber sell services; they do not focus on the reselling of products. Indeed, the sharing economy is gaining support and fundamentally altering how people own and consume property, goods, and services. Network technologies, social and collaborative software, and consumers changing habits all aid the growth of the sharing economy. While the shift toward more sustainable modes of consumption represents a major threat to a number of established business models and revenue streams, it also offers several pathways where companies can benefit. Assisting people in their attempt to share does not necessarily mean they will not buy your products. As Patagonia and Ikea have demonstrated, providing support for sharing enhances not only company support but also its status. Ultimately, the sharing economy creates a more efficient use of physical assets in an evolving form of commerce. The sharing economy takes the philosophies of eBay and craigslist a step further. Participants do not relinquish ownership rather they share it.

Overview of Airbnb

Airbnb was founded in August 2008, headquartered in San Francisco, CA, and is privately owned by Brian Chesky, Joe Gebbia, Nathan Blecharczyk, and Laurence Tosi. It is a website for people to list, find, and rent lodging. It has over 1,500,000 listings in 34,000 cities and 190 countries. Since then it has served over 30 million guests. Such platforms disrupt traditional hospitality industries by creating new sources of supply.

10 Ibid., 15.
11 Ibid., 15.
12 Ibid., 16.
15 Ibid., 71-77.
16 Ibid., 71-77.
17 Yeung, Ken, 2014 "With 8.5m guests, Airbnb seeks to build a more uniform customer experience via its Hospitality Lab.” The Next Web: http://thenextweb.com/insider/2013/09/17/with-8-5m-guests-airbnb-seeks-to-build-a-more-uniform-customer-experience-with-its-hospitality-lab/
trust to maximize the likelihood of a successful booking.\textsuperscript{21} Airbnb has changed the traditional market for tourism by providing an online marketplace that permits large-scale rental of spaces from one ordinary person to another. With this peer-to-peer interaction, the Airbnb website secures its customers identity by ensuring that all members provide photo identification, authentic phone numbers, and links to Facebook and LinkedIn accounts.\textsuperscript{22} With its easy access website, Airbnb is changing the travel economy around the world. A basic overview of how Airbnb began follows in Figure 2.\textsuperscript{23}

Figure 2

Airbnb runs on a marketplace platform model where it connects hosts and travelers and enables transactions without owning any rooms itself. Airbnb’s business model includes minimal regulatory controls in most locations where hosts and guests both have to build trust to create a successful booking. Airbnb’s reputation and revenues have rapidly grown since it was created.\textsuperscript{24} Much of its revenue comes from service fees from bookings. Depending on the size of the reservation, guests are required to pay a six-twelve percent nonrefundable fee.\textsuperscript{25} A bigger reservation has lower service fees for guests. With each booking, hosts are charged a 3 percent fee to cover processing of guest payments.\textsuperscript{26} When booked, guests pay the service fee unless a host cancels or retracts from the listing. Furthermore, depending on state or country laws, customers may need to pay a value-added tax (VAT).\textsuperscript{27} A VAT is a tax assess on the final sale of goods and services. Airbnb guests in the European Union, Switzerland, Norway, Iceland, and South Africa all have a VAT and service fees.\textsuperscript{28} Thus, Airbnb makes much of its revenue from booking fees and from host and guest service taxes.

Airbnb exists in a highly popular economic sector: travel. Because traveling includes a wide variety people for different reasons, Airbnb has competition from the hotel industry and from startups similar to itself. Hotels, while regulated in alternative ways to Airbnb, hospitality marks a defining trait of the hotel industry. According to A.K. Sandoval-Strausz in the book Hotel, “Hotels were sophisticated hospitality machines.”\textsuperscript{29} They served the basic purposes as inns and taverns by providing basic needs including food and shelter. Hospitality transformed with the operation of hotels. As hospitality transformed the hotel industry, it relates the sharing economy core pillars as they relate to Airbnb, specifically an emotional connection and trust.

With Airbnb, an emotional connection and foundation of trust between host and guest shapes a

\begin{itemize}
  \item Ibid.
  \item Ibid.
  \item Ibid.
\end{itemize}
guests’ experience whereas in the hotel industry, hospitality helps shape guests overall experience. Hotels have a permanent state of coming and going with constant contact between strangers and the need to establish and maintain contacts and relationships. In the hotel transformation, they began to “[represent] a new paradigm for hospitality.” 30 Host-guest relationships became increasingly impersonal which was suited for a nation to become more mobile. The growing impersonal connection between hotel guests and employees relates to the purely mobile connection between Airbnb hosts and guests. Many Airbnb guests and hosts never meet but are connection through Airbnb’s website and social media.31 Lastly, over decades, hotel managers and workers devised elaborate methods for welcoming, accommodating, and serving the masses of travelers and strangers who passed through and inhabited the nation’s cities. This helped establish American urbanism developed by the constant movement of people, goods, and information. While the hotel industry continues to develop as it redefines hospitality, Airbnb averages almost 22 percent more guests per night than Hilton Worldwide.32 Regardless of hospitality factors, Airbnb continues to grow and compete with the hotel industry.

Airbnb is present in 34,000 cities and in 190 counties. In fact, in eight major U.S. cities Airbnb rates are significantly lower – sometimes the rates are as much as 80 dollars per night – or comparable to hotels including Boston, Chicago, Los Angeles, New York, Portland, Seattle, and Washington D.C. Indeed, Airbnb is also present in London, Sydney, Paris and Toronto. While Airbnb has a large presence around the world, it has competitors with similar foundations in the sharing economy. Other sharing economy members similar to Airbnb are: Homeaway, Flipkey, Onfinesay, VRBO, and couchsurfing. Homeway is a vacation rental marketplace with more than 1,000,000 vacation rental listings in 190 countries, and has 1588 employees. 33 It operates through 40 websites in 22 languages.34 Flipkey is similar to Homeaway yet it is part of a larger company, TripAdvisor. It deals with vacation rentals on Tripadvisor.com.35 Onefinestay, although a start-up, tries to match the hospitality found in hotels with its home rentals. Guests and hosts can become members of Onefinestay and list or rent homes in London, New York, Paris, or Los Angeles.36 VRBO, however, is part of the HomeAway business, the world leader in vacation rentals with over 950,000 listings. It offers a large selection of properties for varying budgets.37 Lastly, Couchsurfing is a website where provides a platform for members to “surf” on couches by staying as a guest at a host’s home.38 Indeed, these competitors pose a threat to Airbnb because it is not the only company in the sharing economy that provides the home rental services. Airbnb is, however, the largest, most popular company to do so.

Airbnb runs in a highly competitive industry – vacation and home rentals. Because of competition from hotels and other startups, Airbnb’s ratings are a critical part in accruing more members and users. According to George Zervas, Davide Proserpio, and John W. Byers in “A First Look at Online Reputation on Airbnb, Where Every Stay is Above Average”, the average Airbnb property rating is about 4.7 stars on a scale from one to five where one is the lowest and

30 Ibid., 143.
33 “HomeAway,” Winter 2016. https://www.homeaway.com/?k_clickid=%c00f753-e433b-6d55-5e3d2f86b161&amp;gclid=CrwK1Apw_C3j38Enijett-JQ52fP3QYfY11171F0Qh6X6aPW311968pSj-f8Wd8nW6oC.tu.web
34 Ibid.
five is the highest. Additionally, Airbnb “[boasts]” that “94% of all properties” have “4.5 or 5 stars.” The paper then contrasts Airbnb’s rating to that of Trip Advisor. With Trip advisor’s average rating of 3.8 stars. Zervas, Proserpio, and Byers come to the conclusion, however, that Airbnb ratings are more inflated compared to TripAdvisor because either individual versus individual rating or because Airbnb stays can be compared to vacation rental stays. The following chart in Figure 3 examines this comparison.

Figure 3: Distribution of property ratings on Airbnb and TripAdvisor. The dotted lines show the distribution means.

Furthermore, this discrepancy in the ratings between the two companies is evident in multiple United States cities as shown in below in Figure 4.

Figure 4: Distribution of Airbnb and TripAdvisor property ratings by US market

While Airbnb gives an assimilated total property rating, individual ratings are only available on profiles, thus Airbnb does not report an overall average. This makes it difficult for hosts to see what kind of guest they may be allowing into their home. The elusive individual ratings draw the success of the individual ratings a question. This is because Airbnb “boasts” their high property rating thus the deliberate move in not making a big deal about individual ratings. Airbnb, as a company, makes it difficult to acquire bad or harmful ratings. Given the short time to give a rating before the option disappear Airbnb is able to control its customers and hosts. First, if a customer has a bad experience then they may not want to immediately report it. This decision, however, blocks them out from making any type of criticism since Airbnb removes the rating option after a certain amount of days. Inferring the questionable individual ratings also stems from multiple posts on Trustpilot about Airbnb’s poor customer service. Guests rating Airbnb as a one star business used words such as “fraudulent host,” “avoid if possible,” and “incompetent company” to describe their disapproval of the company due to its customer

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70 Ibid., 3.
71 Ibid., 15.
72 Ibid., 17.
73 Ibid., 5.
service.46 While Trustpilot is an opinioned blogsite, people planning trips and vacations do read it and bad ratings can have significant influence on future rental choices.

Challenges in Regulating the Sharing Economy

In November 2012, Nigel Warren, a resident of the East Village neighborhood of New York City rented out his apartment for three nights.47 His landlord was later notified of five violations of illegal transient hotel laws resulting from Mr. Warren’s actions that approached 40,000 dollars in fines.48 Because Mr. Warren was not present during the guest’s stay and accepted monetary compensation, he was found to be in violation of the Multiple Dwellings Law.49 Although Airbnb’s terms and conditions did inform hosts of their responsibility to follow local rules and regulations, many users complained that the company was not explicit enough.50 Six months after receiving notice of his violation, Mr. Warren, with the help of Airbnb’s legal team, proceeded to combat the government’s initial ruling, and succeeded in getting his fine knocked down to 2,400 dollars.51 The Environmental Control Board found that because Mr. Warren’s roommate was present during the time of the guest’s occupancy, he was not in violation of the Multiple Dwellings Law.52 Airbnb followed up by including a more aggressive statement in their terms and conditions regarding the responsibility of their hosts to understand the legality of their actions.53

Despite Mr. Warren’s victory, the highly publicized case opened the floodgates for complaints and legal maneuvers against Airbnb’s operations. New York Attorney General Eric Schneiderman announced that his office would look for a path around the protective clause of Section 230, which transferred the legal liability from Airbnb to their individual hosts.54 New York State Senator Liz Krueger, who authored the Multiple Dwellings Law, claimed that many Airbnb listings in New York, sending a clear warning to Airbnb and its users.55

The rapid growth of the sharing economy has transformed the way individuals utilize resources, leading to substantial efficiency gains. Through the services provided by disruptive companies like Airbnb, Uber, and others, consumers can now make fuller use of their most expensive resources, like homes or automobiles. The decentralized structure of the sharing economy has drastically lowered barriers to entry in previously highly guarded industries, such as the hospitality and transportation industry. Individuals seeking new ways to earn money can easily become suppliers on these sharing services by offering up their resources on a temporary basis.56 Consumers also benefit from the increased supply of these resources through lower prices.

The unprecedented business model employed by companies like Airbnb, Uber, and TaskRabbit, and other shared-services companies, has raised serious challenges for regulators.

46 Ibid.
48 Ibid.
49 Multiple Dwelling Law, Art. 1, §4.8(a)
Many of the laws regulators have been attempting to apply to sharing economy companies were written by lawmakers who did not foresee the development of this new type of industry. Prior to the rise of the sharing economy, regulations were divided into two clear-cut categories: those intended for individual citizens and those intended for businesses. The sharing economy has created a third category: “people as businesses.” Furthermore, because many of the industries prone to disruption by the sharing economy are regulated on a state or local level, a uniform framework has yet to be established. Rather, different states and localities are experimenting with different approaches.

This decentralized regulatory approach has resulted in varying ideas on where the line between consumer choice and consumer protection should be. The sharing economy has benefitted consumers with expanded choice and lower prices. However, the unregulated nature of the industry poses public safety threats. The weight that lawmakers grant to each of these factors should determine the extent of the regulation imposed on the sharing economy. Of course, one cannot ignore the powerful voices of the special interest groups occupying the position of the incumbents in the industries that sharing economy companies threaten to disrupt. This presents another important challenge regulators must overcome in devising an effective set of supervisory policies.

While most sharing economy regulation is enforced on the state and local level, developing Internet-based “peer-to-peer” companies have relied on an important federal statute to circumvent prohibitive state regulations. Section 230 of the Telecommunications Act (“Section 230”) offers Internet based companies legal protection from the posts of their users.

The law states, “No provider of user of an interactive computer service shall be treated as the publisher of speaker of any information provided by another information content provider.” That is, sharing economy website like Airbnb and Uber that consist of user posts cannot be prosecuted for content that violates a state law because the company did not directly publish that content. Section 230 does provide an exemption for federal criminal law violations, under which the companies would be liable.

Section 230 was enacted in 1996, when the digital revolution was still in its earliest stages of development. The law served as a crucial source of protection for the earliest Internet companies seeking to disrupt traditional marketplaces. Since the law’s adoption, companies like eBay, Wikipedia, and eHarmony have relied on Section 230 for protection from the posts of its users. Similarly, sharing economy companies like Airbnb and Uber seeking to solidify market share against established incumbents rely heavily on the protections outlined in Section 230.

State regulators, most notably the National Association of Attorneys General (NAAG), have been lobbying Congress to provide an additional exemption for state criminal law violations. Essentially, this small change in the language would open up Internet company executives to criminal liability for their users’ violations of state laws. This type of regulatory scheme exists in Europe, where Internet companies are responsible for user-generated content. The NAAG claims that the expansion of this provision to encompass state laws will allow state prosecutors to investigate child trafficking and prostitution activities currently protected by

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Section 230. However, sharing economy companies fear that the NAAG amendment would result in more prohibitive state regulations against their services. Whether the NAAG amendment will gain traction in Congress remains to be seen. As it stands now, Section 230 protects Internet companies from criminal prosecution from user-generated violations. Thus, regulators have been forced to pursue individual suppliers of the sharing economy goods and services.

Case Study of Airbnb in New York City:

Why New York City?

Because the regulations governing Airbnb vary based on locality, it would be difficult to analyze each and every regulatory approach. We chose to focus the bulk of our case study on the New York City market for the following reasons. Airbnb has an established presence in New York. Between 2012 and 2013, over 400,000 visitors used Airbnb’s services in New York City, and New York City is currently Airbnb’s largest market. Secondly, Airbnb had a long, highly publicized regulatory battle with New York Attorney General Eric Schneiderman. Because New York took a relatively firm stance against Airbnb, the protracted battle revealed many of the arguments for and against regulations on sharing economy companies like Airbnb.

Overview of Relevant NYC Regulations:

In New York City, the Multiple Dwellings Law governs the space Airbnb occupies. The Multiple Dwellings Law outlines the definitions of the different classes of apartment-style residences in New York, along with the rules and regulations pertaining to each. A “Class A” residence is defined as “a multiple dwelling that is occupied for permanent residence purposes” and includes the following:

- Tenements, flat houses, maisonette apartments, apartment houses, apartment hotels, bachelor apartments, studio apartments, duplex apartments, kitchennette apartments, garden-type maisonette dwelling projects, and all other multiple dwellings except class B multiple dwellings.

The law defines a “permanent residence” a “dwelling unit by the same natural person or family for thirty consecutive days or more.” A “Class B” multiple dwelling is one “which is occupied, as a rule transiently, as the more or less temporary abode of individuals or families who are lodged with or without meals,” and includes the following:

- Hotels, lodging houses, rooming houses, boarding houses, boarding schools, furnished room houses, lodgings, clubhouses, college and school dormitories and dwellings designed as private dwellings but occupied by one or two families with five or more transient boarders, roomers, or lodgers in one household.

For “Class A” dwellings, the law allows for the “occupancy of such dwelling unit for fewer than thirty consecutive days by other natural persons within the household of the permanent occupant such as house guests or lawful boarders, roomers, or lodgers.” Additionally, the law permits “incidental and occasional occupancy of such dwelling unit for fewer than thirty consecutive days by other natural persons when the permanent occupants are temporarily absent for personal reasons…provided that there is no monetary compensation paid to the permanent occupants.”

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That is, it is illegal under this provision for a permanent resident to receive payment to rent out their apartment for less than thirty days, if the permanent resident is absent. This presents a major problem for many Airbnb hosts, as will be detailed in the following section.

New York City also levies a hotel room occupancy tax of 5.875 percent, which amounts to about 1 percent of the city’s total tax revenue. New York Tax Law defines a hotel as a “building or portion of it which is regularly used and kept open as such for the lodging of guests. The term ‘hotel’ includes an apartment hotel, a motel, boarding house, or club, whether or not meals are served.” There does, however, exist an important exemption for individuals who rent out their home on fewer than three occasions or for not more than 14 cumulative days during any 12-month period. While there is some controversy surrounding whether Airbnb listings should be subject to the tax, the NYC Department of Finance declared them exempt from the tax. Despite this ruling, Airbnb has publicly offered to pay their fair share of taxes, provided that lower-income hosts remain exempt.

The History of Airbnb in New York:

In October 2013, Eric Schneiderman began his investigation of Airbnb’s presence in New York City, subpoenaing data on 15,000 Airbnb users. This marked the beginning of the highly adversarial battle between Airbnb and AG Schneiderman. Shortly after receiving Schneiderman’s subpoena, Airbnb announced its plans to fight to protect the privacy of its users. Matt Mittenthal, a spokesman for AG Schneiderman, stated that the purpose of the investigation was to “recover millions of dollars in unpaid taxes and to stop the abuse of Airbnb’s site by operators of illegal hotels.” In the same statement, Mittenthal accused Airbnb of “standing up for highly profitable, illegal businesses that make a huge chunk of its corporate revenue.”

Airbnb’s head of global public policy, David Hantman, responded to the Attorney General’s accusations of protecting illegal hoteliers by asserting that “almost 90 percent of [Airbnb’s] hosts have only one listing at it’s the home they live in.” Airbnb publicized the story of Tara Robertson, a widowed Manhattan resident who used Airbnb’s website to make extra money to cover her expensive medical bills. Ms. Richardson, in a video launched by Airbnb, declared that New York officials were “stepping over dimes to pick up nickels,” alluding to their emphasis on hotel tax dollars and disregard of the overall economic prosperity Airbnb brings to New York. Airbnb’s users also revealed their opposition to AG Schneiderman’s investigation, gaining nearly 20,000 signatures on a petition asking the state senate to reverse the Multiple Dwellings Law in Airbnb’s favor. Because the law, written before Airbnb became popular in

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78 Ibid
80 Ibid.
81 Ibid.
82 Ibid.
83 Ibid.
New York, had the intent of combating slumlords operating illegal hotels, Airbnb and its supporters argued that the legislature should create a exemption for Airbnb hosts.86

Airbnb filed a motion to quash the Attorney General’s subpoena, arguing that it was “without factual basis, overbroad and unduly burdensome.”87 In response, the Attorney General’s Office submitted the affidavit of Sumanta Ray, Director of Research and Analysis with the Investor Protection Bureau of the New York State Attorney General.88 Ray’s findings indicated that while a majority (88 percent) of Airbnb hosts listed only one property, the 12 percent that listed more than one accounted for 30 percent of the listings on Airbnb’s site.89 Ray also found that a majority of hosts rented their apartments for less than thirty days, in clear violation of the Multiple Dwellings Law.90 Based on this information, AG Schneiderman argued that the state’s investigation was more than a mere “fishing expedition,” as Airbnb had previously asserted.91

In May 2014, the Supreme Court of New York sustained Airbnb’s claim that state’s subpoena was too broad in certain areas.92 On the tax issue, the Court declared many of the Airbnb units violated the hotel occupancy tax, since their “apartments are rented on fewer than three occasions or for not more than 14 days in the aggregate during any four consecutive quarters or any 12-month period.”93 Additionally, Multiple Dwellings Law only applies to cities with a population of greater than 325,000 persons, but the original subpoena did not limit its investigation to New York City Airbnb hosts. In this respect, the subpoena was too broad.94 However, the Court ruled in favor of AG Schneiderman’s office with regard to Airbnb’s argument that the subpoena was overly burdensome.95 Ultimately, the gave the Attorney General the opportunity to narrow down the subpoenas to those hosts who are not exempt from the tax and to those who are violating the Multiple Dwellings Law. In July 2014, Airbnb agreed to provide the Attorney General’s office with the data of 124 hosts who “may be flagrantly misusing [Airbnb’s] platform.”96 Additionally, Airbnb provided “anonymized data” for approximately 16,000 hosts to the Attorney General’s office.97

In October 2014, Attorney General Schneiderman released a comprehensive report outlining the use of Airbnb in New York City. The report contained data on Airbnb listings from 2010 to 2014 and found that 72 percent of Airbnb units violating the Multiple Dwellings Law, as depicted in Figure 5.98

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86 Ibid.
89 Ibid.
90 Ibid.
93 Ibid.
94 Ibid.
95 Ibid.
96 Ibid.
97 Ibid.
AG Schneiderman’s report also calculated the hotel occupancy tax liability from these Airbnb listings roughly equal to 33 million over the four and a half year span.\textsuperscript{99} The report also classified Airbnb’s “commercial users” as hosts who rented three or more units.\textsuperscript{100} Of the Airbnb hosts analyzed, Schneiderman found that 6 percent fell into this category. However, these 6 percent of hosts accounted for 37 percent of Airbnb’s revenue.\textsuperscript{101} Following this discovery, Airbnb publicly stated their efforts to restrict the activity of these commercial users.\textsuperscript{102}

Schneiderman’s report did not mark the end of the legal battle between Airbnb and New York officials. Both the Attorney General’s office and the New York City Mayor’s Office are fighting hard to shut down illegal hotels resulting from Airbnb’s services and to collect hotel occupancy taxes. In November 2015, New York City Mayor Bill de Blasio appropriated 10 million dollars to the Mayor’s Office of Special Enforcement to investigate and ultimately eliminate violations of occupancy law resulting from Airbnb’s services.\textsuperscript{103} Individual crackdowns continue to occur throughout the five boroughs. In February 2016, the Mayor’s Office of Special Enforcement raided a property in Brooklyn renting out rooms for as low as 31 dollars per night.\textsuperscript{104} As long as Section 230 remains unchanged, New York officials will have to continue pursuing individual Airbnb hosts for state law violations.\textsuperscript{105} Eliminating illegal hotels one host at a time costs both time and resources. Before long, New York, along with many other states and localities, will have to develop a comprehensive set of policies to deal with the issues Airbnb presents. The following section outlines a logical policy approach that promotes Airbnb’s positive impacts on hosts, guests, and local businesses, while mitigating the risks the company poses.

**Airbnb’s Stakeholders**

Stakeholders involved in the sharing economy, specifically in rental companies like Airbnb, range from renters and guests to the Federal government. Given the complicated nature of renting out homes in compliance with city and state regulations, the hierarchical structure below shows the connections between each actor.

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\[\text{Ibid., 9.}\]
\[\text{Ibid., 10.}\]
\[\text{Ibid., 10.}\]
\[\text{Ibid., 11.}\]

\[\text{Ibid., 9.}\]
\[\text{Ibid., 10.}\]
\[\text{Ibid., 10.}\]
\[\text{Ibid., 11.}\]
According to this structure, the federal government sits on top. Directly under the federal government lie the states. Between the states and the federal governments overarching rules and regulations guide a broad implementation of Airbnb counties and cities. From these regulations, governors, landlords, and Airbnb set their own regulations to influence Airbnb in either a positive or negative direction. Of course, Airbnb wants to positively influence its position in cities and in its terms and conditions, informs hosts of their responsibility to follow local rules and regulations. Indeed, the compliance between hosts and guests and local governance does not always work smoothly and in some of these cases, Airbnb becomes legally involved as in Nigel Warren’s court case. The involvement of different parties including the state, landlords, and Airbnb influence the relationships between local businesses, hosts, neighbors, and guests. The tier under with local business, hosts, and neighbors are the stakeholders who are directly affected as well as the next level of hosts, guests, and neighbors complicated Nigel Warren’s story. The connections between each actor, for example, hosts relationships with their neighbors and landlord and guests respecting the habits of neighbors and community surrounding the hosts home creates intricate patterns between the stakeholders. Ultimately, each actor influences the others. Local business owners either boutique or restaurant owners, for example, want to benefit from guests dining or buying items. The guests help businesses like these flourish. In turn, however, it is assumed that guests comply with neighborhood and landlord regulations.

How Should Airbnb Be Regulated?

Airbnb brings benefits to many different groups of people. In New York, 62 percent of Airbnb hosts claimed that the money earned from this service helped them stay in their homes. Guests take advantage of Airbnb’s lower prices by extending their stays, thus generating revenue for local businesses. Airbnb does, however, present certain risks, and governments should develop practical and comprehensive policy approaches to address them. But governments should be careful not to stifle the benefits that Airbnb brings. This section will outline the specific risks posed by Airbnb and recommend a logical regulatory approach that would strike a balance between protecting public welfare and promoting innovation. These policy recommendations are targeted at the state and local policymakers that largely handle zoning regulations. Local and state policymakers are composed of two groups: the elected officials (i.e., legislative and executive branches) and the unelected bureaucratic agencies who enforce the laws. A successful regulatory framework depends on both the legislature’s passing of the law and the agencies’ enforcement of it. Certain recommendations will target Airbnb and other stakeholders who are affected by the company’s presence. As will be shown, many of the issues

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Ibid.
need not legal regulations to be resolved, but rather active participation and compromise by relevant stakeholders.

Effects of Short-Term Airbnb Rentals on Housing Supply:

A major concern of local government officials is the effect of Airbnb on the supply of affordable long-term housing. Because short-term rentals tend to be more lucrative than long-term rentals, officials fear that Airbnb’s presence will entice landlords to increase short-term rentals, thereby limiting the supply of affordable long-term housing. Lower supply translates to higher prices. Research on the Los Angeles housing market describes how the presence of Airbnb and the growth in short-term rentals has effectively driven up rent prices, particularly in gentrifying neighborhoods. The crisis is particularly severe in cities like Los Angeles, where vacancy rates are near zero. When long-term residential options are converted into short-term rentals and effectively taken off the market, it causes a sudden supply shock. The nature of the housing market is such that increasing supply requires substantial investments in terms of both time and capital, exacerbating the effects of the supply shock. In Los Angeles, the wealthiest neighborhoods see the greatest Airbnb short-term rental activity. The supply shock and subsequent rent spike as described above forces middle-income renters out of these neighborhoods into adjacent lower-income ones. The influx of middle-income renters into gentrifying neighborhoods, prices out the lower-income individuals who previously occupied those areas. In one year, rents increased by over 7 percent in gentrifying neighborhoods in Los Angeles, and by over 9 percent over the course of two years. New York officials fear a similar outcome.

According to Attorney General Eric Schneiderman’s report on Airbnb in New York City, almost 2,000 individual units were rented out for short-term use for at least six months of 2013, deeming them unavailable for long-term purposes. Furthermore, the proportion of short-term rentals in New York increased each year from 2010 to 2013, as shown in Figure 7. As shown in the charts, the share of rentals used for short-term purposes for six months or more increased from 18 percent of rentals in 2010 to 38 percent in 2013.

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110 Ibid., 237.
111 Ibid., 237.
112 Ibid., 230.
113 Ibid., 240.
114 Ibid., 240.
115 Ibid., 240.
116 Ibid., 242.
118 Ibid., 12.
119 Ibid., 13.
120 Ibid., 13.
The geographic distribution of these short-term rentals has been another cause for concern for city and state officials. In New York, many of the short-term Airbnb listings fall outside the highly commercialized areas like Times Square. Rather these rentals are often in residential neighborhoods like SoHo and Williamsburg, Brooklyn. Like the Los Angeles case, middle-income renters may become forced out of these neighborhoods into cheaper areas. The gentrification of those neighborhoods will then drive up housing prices for New York’s lowest-income renters.

The data presented in the Attorney General’s report on Airbnb in New York show that short-term rentals resulting from Airbnb’s services are in fact increasing. However, the increase in the number of short-term rentals may not necessarily translate to the limited supply of long-term housing. Individual tenants renting out their own apartments for a few days at a time when they are out of town pose little threat to the long-term housing market. In New York, 87 percent of hosts fall into this category. Those who pose a formidable threat to the supply of affordable long-term housing are the hosts who list multiple properties on Airbnb, defined as “commercial users” by Attorney General Schneiderman’s office. In New York, these “commercial users” accounted for only 6 percent of hosts, but 36 percent of all reservations made between 2010 and 2014.

An effective policy approach would target these types of users and limit the number of listings they can put on Airbnb’s site. Airbnb should cooperate with government officials in limiting these “commercial users,” as they have stated they would in the past, for several reasons. First, affordable housing is one of Airbnb’s core values. Airbnb was founded in 2007 by individuals seeking to make housing more affordable in San Francisco. Second, without a new set of policies written with Airbnb in mind, city and state officials, like those in New York, will continue to pursue individual hosts. The experiences of Nigel Warren will become far too common, except Airbnb will not realistically be able to step in on behalf of every host facing fines and penalties. Individual hosts will soon become afraid to list their apartments on the website and Airbnb’s entire trust-based business model will collapse. Airbnb should work with governments to include provisions in laws like the Multiple Dwellings Law allowing for individuals to rent out their own apartments on sites like Airbnb. In return, Airbnb should limit the number of listings an individual can place on the site. While this might hurt Airbnb’s revenue stream in the short term, it is a logical way for the company to preserve its business model and its operations as a whole.

Another feasible alternative, as proposed by Dayne Lee, would involve a community benefits agreement (CBA) model, where key stakeholders collaborate and compromise in order to solve the issue of affordable housing supply. Under this model, Airbnb and property developers looking to build and capitalize off of short-term rentals could work with New York’s government to prevent an affordable housing crisis. Lee notes the possibility of property owners


131 Ibid., 10.

132 Ibid., 10.
or developers setting aside a set amount of units in newly constructed apartment buildings as affordable long-term housing options, while reserving others for short-term renters. Governments and developers, under this proposal, could work together to expand the total supply of housing, allowing room for both short-term renters and long-term residents. This plan also aligns well with Airbnb’s core values of promoting affordable housing. Airbnb would capitalize off of the public relations opportunities. This plan provides a feasible way for individuals to take advantage of Airbnb’s unique business model, while making housing more affordable for low-income renters.

Insurance and Safety:

The issue of safety has come up time and again in the debate on how to regulate Airbnb and other sharing economy companies. From the point of view of a host, the idea of having a stranger stay unaccompanied in your apartment may seem strange. Equally strange is the idea of actually sleeping in a stranger’s bed. People worried about theft, destruction of property, or even kidnapping may argue that staying in a hotel is much safer than staying in an Airbnb apartment. Stories of foul play in Airbnb rentals have become highly publicized. For example, in 2014, a resident of Glendale, California using Airbnb to rent out his home as a “party house” caught much news coverage. While these incidents are few and far between and do not characterize the vast majority of Airbnb experiences, they need to be addressed. Failure to do so will not only compromise public safety, but will also undermine Airbnb’s business model.

Airbnb largely relies on self-regulation between its users in order to ensure safety and reliability. All users must make a profile and both hosts and guests receive public ratings and comments from past rental experiences. Most importantly, hosts have the right to deny potential guests if their ratings are not up to snuff. In order to increase the reliability of this internal review system, Airbnb enacted several important changes to the system in July 2014. For instance, in order to prevent retaliatory actions in response to a bad rating, hosts and guests receive notice of their ratings at the same time. The company has also shortened its review period to guarantee that experiences are fresh in the minds of the rating party. Lastly, Airbnb’s new review system asks guests to specifically share one thing they loved about the experience and one thing they wish to see improved. All of these reforms serve to provide honest and informative feedback on Airbnb listings, ultimately improving the safety of users.

Self-regulation certainly has its benefits. The marginal costs of implementation and enforcement are low, and Airbnb’s growth and success speaks to the merits of self-regulation. Its business model is based on trust between its users; if users feel unsafe, they will elect not to use the service. That is why, according to Steve Webb of Turo, a car-sharing service, sharing economy companies have an incentive to adhere to safety regulations even stricter than those imposed by the government. Without building a high level of consumer trust, sharing economy companies like Airbnb and Turo cannot seize market share from established incumbents. However, Airbnb’s success relies on more than trust between hosts and guests. There are other stakeholders on whom Airbnb’s business model depends, namely insurance companies. Companies providing renter’s or homeowner’s insurance take on added risk when homes or apartments they insure are being rented on sites like Airbnb. Airbnb has attempted to

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132 Ibid., 251.
135 Ibid.
136 Ibid.
137 Ibid.
address this issue through its “Host Protection Insurance Plan,” which covers up to 1 million dollars in third-party claims of injury or property damage. The “Host Guarantee” policy, which acted as a supplement to primary homeowner’s or renter’s insurance. The “Host Protection Insurance” plan was intended to be a more comprehensive policy, addressing the gaps in the “Host Guarantee” policy. However, the “Host Protection Insurance” policy has several important flaws. For example, a closer look at the “Host Protection Insurance” indicates that all claims must be filed within 14 days, hosts must be in compliance with all other Airbnb terms in order to receive a reimbursement, and hosts must attempt to resolve the conflict with the guest before filing a claim, to name a few. Furthermore, and perhaps most important, claims must be filed with a renter’s or homeowner’s insurance companies prior to claiming loss under the “Host Protection Insurance” policy.

Insurance companies have taken steps to limit their exposure by refusing to cover Airbnb hosts. Julie Pfeffer, a Delaware resident and Airbnb host, ran into some trouble with her homeowner’s insurance provider, State Farm, after disclosing her activity as an Airbnb host. Despite Ms. Pfeffer’s long history as a low-risk homeowner with State Farm, the insurance company no longer wanted to take on the additional risk. State Farm offered to sell Ms. Pfeffer a commercial policy, since she was in essence using her home as a place of business.

However, that policy was much more expensive and would consume the profits she made as an Airbnb host. Considering that Ms. Pfeffer’s insurance company viewed her as a good customer, it is hard to imagine how an insurer would respond to a less reputable client. Of course, Airbnb hosts can choose not to disclose their commercial activity, but if and when these details are exposed, insurance companies would likely be even less forgiving. Unless Airbnb works with insurance companies to form more comprehensive plans that shift the risk away from the insurers, hosts may find themselves subject to higher premiums or no coverage at all. Higher insurance premiums would cut into the profits of Airbnb hosts and the threat of termination would likely deter them from using the site at all. Insurance companies, thus, play an important role in the success of Airbnb and Airbnb needs to formulate a better policy to address insurers’ concerns.

Airbnb’s self-regulation scheme lends little consideration to the externalities its services impose upon the communities in which Airbnb operates. For example, neighbors may become frustrated with unruly vacationers and landlords and property managers may respond by banning Airbnb-related activities in their buildings. Airbnb’s reputation-driven success relies on incorporating important stakeholders in order to form practical solutions that limit these externalities, while maintaining the innovative and beneficial services Airbnb delivers. A policy of “regulated self-regulation” would accomplish this. Under this model, a committee consisting of relevant stakeholders (i.e., Airbnb executives, state government officials, homeowners’ associations, condominium boards, insurance executives, etc.) would enter contractual agreements to regulate Airbnb’s activities within a city or state. The committee’s policies would be bound by the contractual agreements between its members, thus giving them weight and enforceability. This idea of committee-driven regulated self-regulation adds a sense of
transparency to the policymaking process. Each represented interest thus has an added incentive to contribute practical ideas that would serve the public good.

Airbnb’s unique business model presents a plethora of regulatory issues that if unsolved, can compromise both public welfare and Airbnb’s future success. Therefore, Airbnb has an incentive to work with regulators to create feasible and pragmatic solutions. Airbnb and its users, however, should be optimistic, as many policy alternatives exist to mitigate the company’s risks to public safety, while preserving the innovation and efficiency that has brought benefits to so many of its users.