Uber and his brothers (13.02.2015)

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Disruptive innovations are meant to decrease transaction costs, fostering changes both on the behavior of market actors and on regulatory frameworks. To hinder the development of such exchange platforms is wishful thinking and surely it harms consumers. The Uber case.

Technology and transaction costs

Uber success, whose platform allows users to book a ride and pay for it with a few taps on the smartphone, must be considered within the rapidly evolving process of ICT and the quantum leap of its applications enabled by modern mobile phones and localization features.

ICT "disruptive" innovations are meant to decrease to a large extent transaction costs, the real barrier between potential businesses and a deal that takes place for real. In doing so, disruption can transform potential markets into real ones, it can wipe out business-as-usual scenarios and imposes brand-new challenges to national and local regulators. Market actors on the other hand are forced to innovate and some of them, those protected so far by a regulated framework, are at a critical turning point.

In the specific case of car rides, the starting point is that the greater part of drivers everyday have free places during rides already scheduled for individual needs, while there's surely a certain number of people going along the same route who would benefit from a lift. Enter Blablacar, the online platform that matches specific and quasi-real time users' supply and demand, something not even conceivable just a few years ago, when rides were requested and offered only in the small circle of friends and family or hitchhiking. In such cases the service quality is very relevant and in fact it is usually evaluated ex-ante on the online platforms, usually through a reviewing system. Uber app for instance enables users and drivers to mutually review each other, with a 1-to-5 star reviewing system. Bad reviews for users can result in a longer waiting time, but for drivers they might result in being kicked out of business.

The economic nature of Uber service

Uber is pretty different from other activities it is sometimes not appropriately compared to. Blablacar for instance properly qualifies as "sharing economy", it is related to a ride and a route autonomously decided by the driver, a ride that would have happened anyway and that is only occasionally shared. The service emerges from an opportunity originated by an individual need that takes priority over everything else. In the food sector, a proper "sharing economy" activity could be implemented sharing our food surpluses (whose inelegant version is of course "left-overs") with indigent strangers. In fact if surpluses are scheduled and intentionally produced so as to sell them, this is simply a standard service, typically offered by a catering company. In parallel, Uber enables users ("customers" would be a better definition indeed), to benefit from a customized transport service, not certainly emerging from an unintentional surplus.

Uberpop drivers are just reimbursed, but the amount, at least on urban routes, could hide a profit, should we assume that the cost of the vehicle is a sunk cost and that marginal operational costs are certainly smaller. On the contrary Blablacar drivers can hardly cover their travel expenses. Uber, as Airbnb in the house rental sector, can not be classified as "sharing economy", it should be better defined as an example of "dormant assets economy", i.e. services and goods that after a long time have been made available by the sudden decrease of transaction costs.

Technology innovation and regulation

Criticized worldwide by taxi drivers for unfair competition, Uber service portfolio is broad and fits all budgets: from Uber Black, a premium service from professional drivers with luxury cars, to Uberpop that enables any non-professional driver to offer lifts to users registered on the Uber platform. UberBlack is not compliant with some specific parts of the Italian legislation related to car rentals with drivers, e.g. the obligation to return to the garage after each ride. Nevertheless the Italian antitrust authority is in favour of the liberalization of such services, so as to make standard taxi services and car rentals with driver perfect substitutes. In December 2013 the District of Columbia, US, has defined a new category for drivers active in the so called "*digital dispatch*" arena, establishing ad hoc user charges based on time and distance, harmonizing the license needed to offer taxi and standard or luxury car rentals with drivers and finally pushing the local *Taxi Commission* to issue new licenses. A few US cities have defined specific barriers to protect regulated incumbent operators: New Orleans and Vancouver have established a minimum fare, other cities have set a limit on the number of licenses (the big primordial mistake of linking the personal asset of the taxi driver to the obtainment of a license) for luxury car rentals with a driver, Miami has applied both systems.

Uberpop faces more challenges, currently banned in Belgium, France, The Netherlands and Spain (and in Italian cities like Torino) because of the non –compliancy with national transport policies and consumer protection. The keystone, in this specific case, could be the creation of stricter controls on drivers and insurance conditions. The Public Utility Commission of Colorado and California in the US followed this path, and set up a minimum threshold of $1m for the liability car insurance in case of ride-sharing. Airnbnb instead has been criticized firstly because of the lack of health and safety compliancy of flats and rooms for rent and also for the absence of formal guest registration that could result in a significant decrease of fiscal revenues – such as the tourist tax - for local administrations. Amsterdam City Council came to the regulatory decision to ask registered hosts to pay all local taxes.

Revenues and tariffs

Airbnb valuation today is around $10b, against Uber 41 billion which has more than doubled in the last semester, also thanks to a business model that can quickly scale and expand geographically, transferring the risk on to drivers.

These companies operate with a fee: 20% on each ride for Uber, Airbnb shows a range from six to twelve percent for each booking. In 2013 Uber and Airbnb revenues topped $165m and $250m respectively.

From the fiscal point of view, Uber drivers in Italy (like Italian Airbnb hosts) must pay income taxes, whereas corporate taxes on revenues are collected in The Netherlands for Uber and in Ireland for Airbnb. Governments have been trying recently to internalize the taxation of foreign company profits, applying the so called "permanent establishment" rule according to which a firm making business in one OECD country must pay the taxes levied on the net profits generated by the local business to the country where it operates. Currently Google's dispute in Italy, so as to tax locally the revenues from its advertisement business, is a good example.

Concerning tariffs, Airbnb hosts are free to decide what to charge users for the rental of flats, houses or rooms. Uber on the contrary, defines its own tariff system, variable from city to city and composed of a fix amount and a variable amount (function of the ride time and distance). Although the tariff spread between traditional taxi service and Uber varies geographically, usually UberBlack is a premium service, and thus is more expensive. It's not straightforward to evaluate Uberpop against the taxi, it seems in fact very linked to the time and the location. Uber tariffs are more expensive in peak hours, such as weekend or holidays, with surge tariffs 7-8 times the normal rates. In the US, the company was harshly criticized for the application of surge pricing during extreme weather events, as Hurricane Sandy in 2012. In order to avoid similar situations, the company made an agreement with the State of NY to cap surge pricing, with a "*multiple of the base fare […] to be determined […] based upon the price set by Uber for the same transportation option, in the same city and surrounding area, during the sixty days preceding the commencement of the abnormal disruption of the market*".

What is next

We can't foresee the future of Uber operations in Italy, nevertheless it is certain that the narrow-mindedness against strategically disruptive technology can be just short-lived, like a totally unsuitable downstream water barrier. Meanwhile, exchange platform prevention surely harms consumers. Even traditional stores face greater competition today compared to the past, and Ebay and Amazon are just the most known examples. If we say no to Uber, shouldn't we oppose them as well?

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