Sharing Economy in Lithuania: Lessons of Success and Failure

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The sharing economy is becoming the next big thing. To recap briefly, it is a type of business model where the online platform enables buyers and sellers to communicate directly. The market players are usually (but not exclusively) people who work on a freelance basis. In addition, digital platforms usually provide various tools like direct contact options, feedback and payment systems, etc.

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According to the European Commission, in 2015, the gross revenue in the European Union from collaborative platforms and providers was estimated to be EUR 28 billion. In the United States, nearly 1% of adults actively earn income from the online platform economy. Nevertheless, compared to the last three years, this number has increased tenfold. The total number of people who have used sharing economy platforms has increased forty seven times in the last three years. Even though the numbers are still not significant, the recent increase has been immense. Taking this and other factors into consideration, the European Parliament estimates that the potential economic gain from the better use of capacities enabled by the sharing economy is EUR 572 billion in annual consumption across the EU.

The first sharing economy businesses appeared in Lithuania only a couple of years ago. Therefore, there is not enough economic data to evaluate how significant it has been to the Lithuanian economy. The sectors that the sharing economy business models emerge in are rather different and completely separated. This has led to both – different attitudes of the governmental institutions and different paces of development. In order to see how sharing economy markets operate, an analysis of the relationship between the governing bodies and the sharing economies is much needed.

TAXI REGULATIONS IN LITHUANIA

The main passenger transporting companies in Lithuania are taxi companies. Taxi drivers and their cars are subject to a certain set of rules and requirements. As in most of the countries, special marking signs are required for cars. These include a taxi sign which has to be placed on top of a car and has to be lit while the car is being used as a taxi. A car must also have a specific yellow and black marking on the outside of it. Requirements for taxi cars also include specific license plates and more strict civil insurance policies, which tend to be more expensive than the ones for regular cars. Moreover, taxi cars have to pass a vehicle inspection once a year, and twice a year if a car is older than five years.

> SEEING THE NEW P2P LENDING PLATFORMS AS THE SAME TYPE OF SERVICE PROVIDERS, THE BANK OF LITHUANIA TOOK A RIGID STANCE ACCUSING THE FIRST PLATFORMS OF ILLEGALLY PROVIDING INVESTMENT AND PAYMENT SERVICES

The drivers themselves must have a municipality-issued license and a certificate which confirms that the driver has passed a government-organized examination for taxi drivers. Taxi drivers must also carry out a meticulous journal logging system which has to be synchronized to a registered taximeter. Needless to say, issuing of these taximeters is charged extra by local taxing authorities.

Despite the fact that some of the taxi companies have been under investigation for tax fraud, compared to other countries, Lithuanian regulations for taxi drivers are less restrictive. For example there is no limitation of the number of taxi cars or drivers, and the license fees are not as exorbitant as in Paris or New York. Although the cars are required to have a certain visual marking, the requirements are not as specific as, for example, the ones in London.

UBER IN LITHUANIA

Uber flourished in part due to being able to suggest an alternative to the aforementioned excessive regulations throughout the world. Yet, this has not been the case in Lithuania. Uber reached Vilnius on January 2014 by establishing its branch office in the city. In October 2015, the Vilnius Municipality and Uber signed a joint agreement to commence operations. By the end of 2015, the company was already providing services for drivers and riders alike. According to the Logistics and Operations Manager for Uber Lithuania Vytautas Černiauskas, Vilnius has been the fastest city in which Uber has established its services so far.

On the one hand, such a hasty introduction of the service had its benefits. It provides opportunities for people to earn money by driving, and riders have more options of services. On the other hand, the business model encountered uncertainties with the legal system. At first, this discouraged


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some drivers from taking up new business. However, the support from the Mayor of Vilnius and the Prime Minister resulted in clearer taxation rules, which encouraged more people to join Uber both as drivers and riders.

OTHER RIDE-SHARING EXAMPLES

The smooth and swift establishment of Uber produced negative feedback as well. Taxi drivers, similarly to their counterparts in other countries, started protesting a new ride-sharing competitor. But contrary to their colleagues abroad, Lithuanian taxi drivers did not end up rioting. Mobile taxi hailing apps saw the possibility and copied Uber's business model. So now, most of the taxi apps also act as ride sharing platforms with drivers working in a similar manner to Uber. This happened due to three main factors:

1. The Lithuanian government was welcoming towards new innovative business models, especially Uber.

2. Regulations applicable to a traditional taxi business were not particularly excessive. This means that taxi drivers did not have to invest significant amounts of money in their taxi business. This led to a more stable shift in[1] the business model. The ICT infrastructure of taxi hailing apps was already developed enough. Only a slight adjustment in app design and business organization was necessary to adapt to a new model.

FUTURE REGULATORY MODEL FOR RIDE-SHARING

The fast development of ride-sharing business models has led to a implementation of a legal vacuum in this area. The Lithuanian Parliament is discussing a new amendment to the Lithuanian Road Transport Code which would add more legal certainty in the field of ride-sharing. A new regulation that will most likely be adopted will allow drivers from Uber and other ride-sharing companies to continue to provide services for customers without any additional licensing requirements. This means that the ride-sharing services should flourish in the future due to a favorable regulation. On the other hand traditional taxi services might find it harder to compete. If regular taxi companies will not reinvent their businesses they will most likely lose a part of their market share to ride-sharing businesses.

P2P LENDING IN LITHUANIA

The first digital P2P lending platform in Lithuania started its operations on August 2014. By the time P2P lending companies started their businesses in Lithuania, consumer credit or "payday" loan companies had already been viewed as problematic by the main Lithuanian banking sector regulatory body. The Bank of Lithuania felt that some pay-day borrowers lacked responsibility. Seeing the new P2P lending platforms as the same type of service providers, the Bank of Lithuania took a rigid stance accusing the first platforms of illegally providing investment and payment services. The allegations have been dropped, but all the P2P lending platforms were made to register as consumer credit companies.

The ongoing negative attitude towards payday loan companies and a failure to separate P2P lending platforms from consumer credit services have resulted in a harsher Lithuanian Consumer Credit Act regulating P2P lending platforms as well as payday loan companies. In early 2016, a new law created a new set of

[1] It has to be noted that the Lithuanian Bank does not separate P2P lending platform data from payday loans, therefore the absolute numbers given in the statistics do not represent P2P lending platforms directly. Nevertheless, the relative numbers partially describe the P2P lending situation because it has suffered similar losses.

market entry barriers and service limitations that have affected the market significantly.

Among a set of bureaucratic procedures, P2P lending platforms are now required to have business sustainability plans and customer creditworthiness evaluation methodologies. Even though it may sound benign, there are no clear guidelines which define what business plans will be deemed sustainable or which creditworthiness evaluation methodologies will be deemed acceptable. Apart from that, significant procedural restrictions for consumer credits have been implemented as well. Both consumer credit companies and P2P lending companies have to check the creditworthiness of a customer and issue a credit only if a customer has a debt to income ratio lower than 40%. What is more, new debtors have to obtain consent of their spouses to borrow resources. Specific P2P lender restrictions have also come into power. Lenders can only give EUR 500 worth of credit to one borrower in a period of 12 months. Furthermore, a total amount of credit received by one creditor cannot exceed EUR 5,000 in a period of 12 months.

EFFECTS OF P2P LENDING AND CONSUMER CREDIT REGULATIONS

New regulations have impacted the consumer credit and P2P lending markets significantly. According to the Bank of Lithuania, in one quarter after the new legislation came into power, the number of loans that are overdue by 60 days have decreased by 12%. In Q1 of 2016, a total amount of 441 thousand consumer loans was issued. That is 21% less than in the end of 2015. All in all, both the number of newly issued loans and the total value of credits have dropped[2] due to a number of new restrictions and regulations. Despite the fact that the government is trying to curb both the consumer credit and P2P lending sector, new platforms are emerging. Since the establishing of the first lending platform in 2014, the total number of platforms has reached four, but the liveliness of the market is still far from what is happening in the UK. The vast majority of the P2P lending activity is concentrated there. It accounts for over 84% of the entire European market, while Lithuania accounts for less than 0.1%.

FUTURE REGULATORY MODEL FOR P2P LENDING

Neither the Lithuanian government, nor the society distinguishes between the P2P lending sector and the payday loan businesses. This is the main reason why the P2P lending sector will most likely remain regulated as strictly as the consumer credit market. Nevertheless, P2P lending companies fight actively against the current regulation. This has resulted in a proposal to abolish limits on the amount of money invested by lenders and the amount of money borrowed by debtors.

Despite the fact that the P2P lending platforms are being frowned upon by the government, a new legislation is being proposed by the government which enables crowdfunding activities in Lithuania. It will allow both natural and legal persons to acquire funds for funding of their future businesses, as well as professional, scientific or research projects. New legislation will most likely have some traces of paternalist regulations that the current Consumer Credit Act has. For example, it is most likely that the creditors will be able to invest only up to EUR 1,000 using one crowdfunding platform. A new legislation is expected to be adopted in late 2016.

REGULATION OF HOTELS IN LITHUANIA

Lithuanian hotels are subject to an extensive set of different rules. They consist of various requirements for the construction

[2] http://www.lb.lt/sugrieztinus_vartojimo_kreditu_teikimo_salygas_ju_suteikta_gerokai_maziau

> ONLY A COUPLE OF YEARS AFTER THE LAUNCH OF HOME-SHARING PLATFORMS IN LITHUANIA, INTENTIONS TO REGULATE IT HAVE EMERGED

including: water and electricity supply, sanitation, telecommunication, accessibility for the disabled, lighting, ventilation and fire safety standards. Apart from that, there are specific requirements regarding being soundproof and the temperature level in hotels (at least +18°C). Finally, hotels must also pass sanitation inspection. Both the intensity and extensity of the sanitation standards depend on whether the hotel has a restaurant in it.

Aside from all the aforementioned requirements, some of the hotels are subject to a mandatory "pillow-tax". The Lithuanian pillow-tax system is set by municipalities; therefore the taxation varies by the regions. Usually, a certain tariff is set for accommodation. This means that a customer of a hotel usually has to pay an extra amount of money per night.

HOME SHARING IN LITHUANIA

Home sharing in Lithuania is not a new concept. People living in resort towns rented out their flats, houses or any real estate as a short term accommodation to the vacationers long before the IT platforms were developed. Only after around twenty five years the concept of home sharing was elevated into a digital level. It is difficult to estimate when the online home-sharing platforms were first used in Lithuania. One of the most popular platforms, Airbnb.com, does not have its branch office in Lithuania. Another similar platform, booking.com, was established in Lithuania in 2014.

It is difficult to estimate how many people use these platforms for their businesses as they are not eligible to register as the accommodation providers. Booking.com has over 2,000 listings in Lithuania whereas Airbnb is said to have over 1,000 listings.

FUTURE REGULATORY MODEL FOR ACCOMMODATION

Only a couple of years after the launch of home-sharing platforms in Lithuania, intentions to regulate it have emerged. The biggest pro-regulation stakeholder appeared to be the Lithuanian Hotel and Restaurant Association which represents already established market players. The association has approached the Lithuanian government with the proposal to regulate short-term home-renting activities including home-sharing platforms. Regulations would require homeowners to provide certificates from governmental institutions confirming that the accommodation meets certain government-set requirements dealing with building safety and hygiene, which the established market players are already subject to. Home owners would be required to meet special fire safety standards, which would be higher than the regular ones applied to typical housing. Above all, new regulations would require all short-term house-renting businesses to register separately with the State Tourism Department. The Lithuanian Hotel and Restaurant Association claims that

the main purpose of such regulation is to calculate the tourism streams in Lithuania more thoroughly. It is also said that the additional regulations will not add to the cost of the homeowners who want to rent out their real estate. This however, may not be entirely true. What these suggestions definitely do add are additional bureaucratic procedures that do not exist at the moment.

Firstly, homeowners would have to get all the necessary certificates from different institutions in order to submit them to the tax administration institution. Secondly, all of the businesses would have to register with the State Tourism Department. These procedures would add up to a cost of small businesses.

Other significant changes would come with the special hygiene, fire and building safety requirements. In order to meet the raised requirements, owners would have to invest more in their real estate. What is more, for example, a hygiene certificate may cost between EUR 44 and EUR 117, depending on the size of the accommodation. And above all, registering with the State Tourism Department would mean that the new businesses would have to pay the aforementioned pillow tax set by the respective municipality. All of these will undoubtedly increase the costs and lower flexibility in organizing home-renting activities and in turn, would result in a reduced competitive advantage now possessed by the new accommodation-sharing businesses.

LITHUANIAN GOVERNMENT: THE GOOD, THE BAD AND THE INDIFFERENT

The presented three areas of the sharing economy and their relationship with the Lithuanian government perfectly illustrate how businesses which share many similarities can be treated completely differently. Firstly, there is Uber and other ride-sharing businesses that have been warmly welcomed in Lithuania. Secondly, there are entities which experience completely different sentiments – namely, P2P lending platforms, which have been a target of heavy governmental regulations. Thirdly, there is the accommodation sector where the main initiative to regulate home-sharing businesses comes from the competitors – hotels. After analyzing these three cases, the following issues influencing the regulation to the greatest extent can be identified:

1. **Prior attitude and prejudice towards similar traditional services**

All of the three cases show that the prejudice of the government and the society is extremely significant when it comes to the forming of the regulatory environment. The ride-sharing and accommodation cases prove that when the government does not have a negative attitude towards traditional services (e.g. taxis or hotels), it most likely will not be inclined to regulate the sharing economy business model rigidly. P2P lending example shows a different side of the coin – the government has considered traditional services (i.e. payday loans) harmful. Therefore, the emergence of a new sharing economy business model has not been considered as a new type of business or a way for people to invest money but rather as an additional possible threat to financial security. This has led to an extensive regulation that prevents a sustainable development in the early stages of the P2P lending development.

2. **Separation of a new business model and similar services**

The ride-sharing case has proven that a distinction between the sharing economy and its traditional competing business is a key to success to not putting it under the same heavy regulatory burden. If a regulatory body distinguishes different business models, it will most likely treat it favorably. However, P2P lending has proven the other side of the story – the Lithuanian governing bodies have not separated them clearly from the consumer credit businesses what led to the same type of rigid regulations.

3. **Stakeholder and competitor activity**

An important issue that has a strong influence on how the future sharing economy regulatory model will develop is the activity of stakeholders and competitors in particular. They influence both the regulation and the markets. The accommodation case shows that the competitors may be on the forefront of regulating sharing economy businesses more harshly. Taxi drivers have tried to do the same, but instead after evaluating the costs of transferring to a ride-sharing business, some of them embraced the change themselves. Taxi companies started providing ride-sharing hailing services on their applications and the taxi drivers started using these platforms.

CONCLUSIONS

The undeniable growth of sharing-economy business models has shown that the consumers are using new services willingly. Therefore the growth will probably continue. The interest shown by consumers is a clear sign to the legislators that the new services are satisfactory and the regulations that have shackled traditional businesses and increased their price have become obsolete. The sharing-economy is a chance for Europe and the entire world to review these legislations and abandon them, making it easier for traditional businesses to compete and for the consumers to get an even wider variety of services. The Lithuanian cases of sharing-economy businesses show different paths which the regulators can take. The cases show that new sharing-economy businesses must not be idle when setting up their businesses. They have to actively work with the government and stakeholders showing them how new services can benefit markets and consumers. ●

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