

Acknowledgements

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Key results at a glance

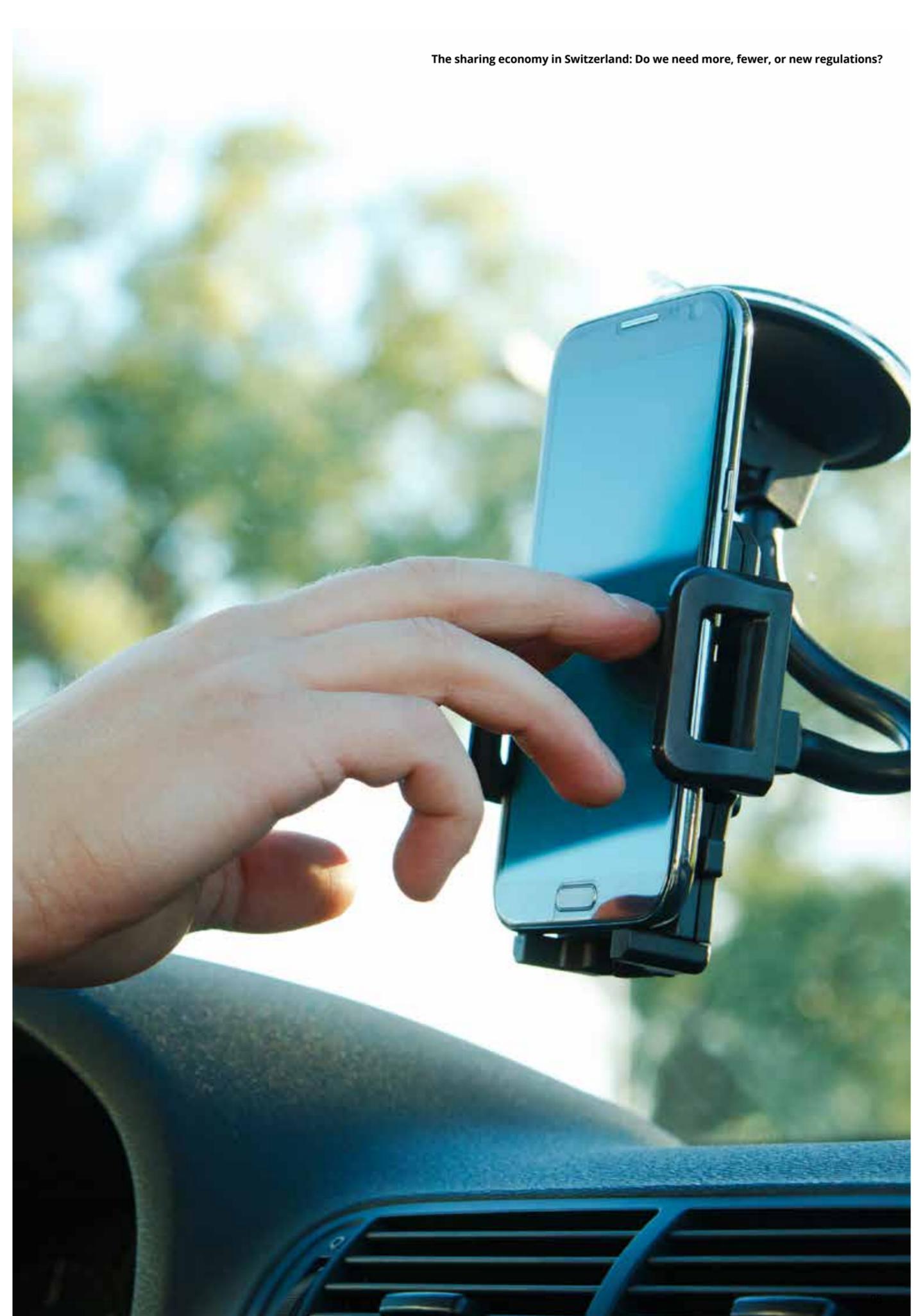
The sharing economy is a growing trend. More and more people are using and offering products and services which are supplied via online platforms. This leads to a more efficient allocation of goods such as cars and apartments, a greater range of goods and services on offer, lower prices and frequently better quality, all of which is ultimately better for consumers. But the sharing economy also benefits private persons who are able to offer their goods and skills to a global network – until recently virtually inaccessible – at low cost and with little risk.

In spite of these advantages, opposition to the sharing economy is on the increase. The huge success of platform operators such as Airbnb and Uber has led to businesses within the “traditional” economy coming under strong pressure. These businesses complain that providers and platform operators in the sharing economy are subverting regulations, and demand that they have to comply with the same regulations as “traditional” businesses, or even demand that they be banned from operating.

Based on the accommodation and personal transport sectors, this opinion paper shows that such demands are exaggerated. While some legal adjustments are needed, consumer protection, which is the purpose of many regulations in the “traditional” economy, can be achieved without state intervention, often more efficiently.

In the opinion of the authors, the following six measures need to be addressed in Swiss legislation. Taken together, they form a kind of regulatory framework for correcting market failure, easing the burden on the “traditional” economy, and ensuring the necessary legal safety:

- **Existing outmoded regulations need to be scrapped:** the sharing economy provides an opportunity to get rid of regulations in the “traditional” economy which have grown up historically and are now outmoded, such as the local knowledge test for taxi drivers and the quantitative restrictions imposed on taxi companies.
- **Statutory legitimacy should be accorded to self-regulation:** statutory legitimacy should be accorded to rating and monitoring systems as a form of self-regulation. Such systems are capable of replacing many traditional regulations (e.g. relating to the cleanliness of accommodation and the reliability of drivers) and can achieve the same aims more efficiently.
- **Minimum requirements should be introduced:** not all problems can be solved by means of self-regulation, and therefore certain minimum legal requirements should also apply in regard to sharing economy platforms, such as the background check on drivers, or the mandatory registration of foreign tourists staying overnight.
- **The legal distinction between “commercial” and “private” activities should be abolished:** since the legal distinction between commercial and private activity is almost impossible to apply to the sharing economy, proven aspects of market failure – in particular, specific hazardous situations – should form the starting points for minimum requirements. For example, the requirement that transport intermediaries (both electronic and traditional) must carry out a background check on their drivers could depend not on whether the service is carried out on a professional basis, but instead – which would accord with the hazard potential – in a general way. In the accommodation sector, certain minimum standards could depend on the number of days for which a property is let. The effectiveness of such regulations should be reviewed periodically and corrected if necessary.
- **Cooperation with platform operators:** cooperation between the authorities and platform operators will make it possible for taxes such as visitors’ taxes to be collected without great administrative cost.
- **Standard digital billing tool for social security contributions:** a similar solution should also be aimed for the provision of social protection for the working population: with a digital tool, the standard billing of contribution rates for social security can be easily achieved both for businesses and for individuals or intermediary platforms. The distinction between the employed and the self-employed would no longer be of prime importance.



Introduction: the origin and importance of the sharing economy

In 2015 the term “sharing economy” made it onto the shortlist for “word of the year” drawn up by the British dictionary service Oxford Dictionaries. This was not unexpected, since the sharing and hiring of goods and services via online platforms has been a growing trend for some years. The flagships of the sharing economy include companies like accommodation platform Airbnb and Uber, the transport service intermediary. According to a European Union study, the sharing economy in the EU had a turnover of EUR 28 billions in 2015, almost double the figure for 2014.¹

The principle of sharing and hiring is not in itself a new phenomenon. The Swiss car-sharing company Mobility was established back in the 1990s. However, the sharing economy as we know it today only developed seven or eight years ago thanks to digitalisation and the spread of smartphones. In public discourse, the term has been used since then to designate a phenomenon that goes beyond the classic principle of sharing and which is referred to in specialist circles as the “collaborative economy”, the “on-demand economy” and “crowd-based capitalism”. This is a

modern form of the market economy in which transactions (i.e. swapping, buying or exchanging services) can be carried out anywhere at any time via online platforms, made possible by smartphones and tablets. The companies involved no longer operate as conventional “suppliers”, i.e. using their own means of production to create products and services. Instead, these platform operators act mainly as intermediaries between those on the supply side and those on the demand side, who in many cases are private individuals (“peer-to-peer sharing”). Thus private individuals are no longer found only on the “demand” side, but can also become suppliers and therefore “micro businesses”.

Switzerland is also affected by the “sharing” trend. A representative survey carried out by auditing and consultancy company Deloitte shows that 55 per cent of Swiss residents already use the sharing economy, either as suppliers or customers, mostly in the transport and accommodation sectors.² However, demand for the provision of services is increasing: work of all kinds can now be offered to other persons or companies on demand through online platforms. The range of services is wide, extending from data research, design, domestic help and translation to financial and legal advice.

Already enjoying huge success, the sharing economy is only in its early days. The European Union estimates that the sharing economy has the potential to reach around EUR 570 billion in Europe, multiples of the current market volume of EUR 28 billion. Investor interest is correspondingly high: annual global investment in sharing economy start-ups has risen from USD 300 million in 2010 to over USD 14 billion in 2015.³

However, the future prospects for the sharing economy are not all rosy. Although the sharing economy has huge growth potential, it is facing increasing resistance, particularly from the ranks of the “traditional” companies to which it poses a threat. These opponents warn that the sharing economy (i.e. the platform companies) operate in a legal “grey area” and that they are subverting regulations and labour-law standards, and should therefore be more strictly regulated or even banned.⁴

This study examines whether such demands are justified. In the first section, the regulatory framework of the sharing economy is assessed from an economic perspective, the central question being which regulations are expedient as far as the national economy is concerned. The second section focuses on the legal perspective: how can the economic characteristics of the sharing economy be implemented in law so that the economic benefits can be reaped while safeguarding the regulatory purposes of legislation? Finally, building on these two main sections, potential guidelines for the sharing economy are developed.

The study is confined to the accommodation and personal transport sectors in Switzerland, these two sectors representing the most important areas of the sharing economy in the country. Evidence of this is already provided by the success of the two best-known sharing economy platforms: it is estimated that Airbnb already has a market share of 10 to 25 per cent of overnight stays in the largest cantons, while driving services intermediary Uber now has over 1,000 drivers on its books in Zurich alone.⁵

The sharing economy from an economic perspective

The economic impact of the sharing economy

In the sharing economy, goods and services can be exchanged with people all over the world at the click of a mouse. Any information needed about the product, the supplier and the potential customer can be found with similar ease. This makes possible market transactions that previously would never have taken place because of the excessively high transaction costs involved. In particular, goods that are used relatively rarely by their owners, or at least are not used to their full capacity (such as cars and dwellings), can be hired out more easily thanks to lower transaction costs, resulting in a more efficient allocation of these goods.⁶

The associated expansion of goods and services on offer leads to more intense competition and lower prices, which ultimately benefits the consumer.⁷ In an empirical study of the car sharing market, Fraiberger and Sundararajan show that low income households benefit the most, since they gain access to goods (such as a car) that they could not afford to own.⁸ As well as increasing the options available to consumers and the range of goods and services on offer, the sharing economy also improves the quality of the goods and services.

Rating systems provide information that would be virtually inaccessible to consumers in the “traditional” economy, giving suppliers a powerful incentive to offer higher quality goods and services. Another study, from the United States, finds that the sharing economy improves product quality in the “traditional” economy. Uber’s entry into the market and the resulting competitive pressure has seen “traditional” taxi firms improve their service, resulting in greater customer satisfaction.⁹ Increased consumption and improved quality ultimately leads to economic growth.

There are also welfare gains for suppliers. The creation of peer-to-peer online platforms enables private individuals to offer their goods and skills to a previously almost inaccessible global network at low cost and with little risk, thus earning additional income. However, certain groups on the supply side have suffered welfare losses due to the sharing economy. These groups include “traditional” economy suppliers who have come under pressure from the new competitors and increasing competition, and who have lost market share. However, studies generally indicate that the sharing economy makes the “cake” bigger and by no means merely replaces “traditional” transactions.¹⁰



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1. European Parliamentary Research Service 2016.

2. Deloitte 2015.

3. Owyang 2016.

4. Cf. on this point the demands made by the European hotel association: Hotrec 2015, http://www.hotellerie.de/media/docs/hotrec_policy_paper_on_the_sharing_economy_final_02112015.pdf, taxisuisse 2014, <http://www.astag.ch/upload/docs/ASTAG/140911-MM-taxisuisseMarktbedingungen-d.pdf> or Hasler and Koch 2015.

5. Walliser Tourismus Observatorium 2015.

6. Edelman and Geradin 2015; Haucap 2015.

7. Benjaafar et al. 2015; Fraiberger and Sundararajan 2016; Fremstad 2014.

8. Fraiberger and Sundararajan 2016.

9. Wallsten 2015.

10. See for example The Economist 2015 or Zervas et al. 2016.

When is government regulation justified?

Despite these economic advantages, there is considerable opposition to the sharing economy. In particular, there are demands from the sectors affected (such as the taxi industry and the hotel industry) that the sharing economy needs to be more strictly regulated or even banned.¹¹ Our assessment of whether these demands are justified is based on classical economic theory, which states that government intervention in the market is above all warranted when markets themselves do not allocate goods and services efficiently.¹² When such “market failure” occurs, government intervention can improve the situation.

Generally speaking, economic theory envisages four causes of market failure: public goods, monopoly power, external effects and information asymmetries.¹³ As far as the sharing economy is concerned, it is the last three that are significant.

- A **monopoly** exists when there is only one seller on a market. Because the single seller can influence the price of goods by adjusting the quantities available, ultimately supply is lower and prices are higher than is optimal for society as a whole.

- **Externalities** describe effects that economic activities have on unrelated third parties, and are not taken into account by the party causing the effects. An example of this is environmental pollution generated when a product is manufactured. Because of negative external effects, the quantity produced is higher than the quantity that would be socially optimal.

- **Asymmetrical information** arises when one side of the market has significantly more information about the market transaction, such as the quality or the condition of an item. For example, the seller of a used car knows more about the condition of the car than any potential buyer. The buyer is aware of this risk and therefore not willing to pay different prices for similar vehicles, since he cannot assess their quality. This can lead to suppliers of higher quality vehicles being forced out of the market, because they cannot ask higher prices than suppliers of poorer quality cars.

In the event of market failure, government can try to increase social welfare by intervening, for example through restrictions, taxes or governmental provision of the item in question. But because the political process can also fail (in which case we speak of a “government failure”), interference in the market mechanism does not always lead to a more efficient result. Reasons for this include a lack of knowledge about the precise economic consequences of a regulation; the behaviour of the administration and of politicians; and the political influence of interest groups.¹⁴ For example, businesses may have a vested interest in regulation if they can use it to raise the entry barriers for competitors. In this case, the regulation in question no longer serves to correct market failure, but merely helps the supplier. As a result of the political influence exerted by many businesses and associations, examples of this type are not infrequently found in practice.

Has market failure occurred in the sharing economy?

In making an economic assessment of the need for regulation in the sharing economy, one must consider whether the causes of market failure mentioned above are present, and, if so, whether government intervention is likely to correct them successfully.

Monopoly power

Since network effects play an important role in the online platforms that dominate the sharing economy, immediately raises the suspicion that companies such as Airbnb and Uber are monopolistic. According to Brühn and Götz, a “winner takes it all” phenomenon can arise, in which the first supplier on the market seems to have all the advantages on his side and it is almost impossible to set up a second similar network.¹⁵ This is because sharing economy platforms are characterised by scale effects: the more goods and services are offered on a platform, the greater the number of people seeking those goods and services will be drawn to the platform, and the more representative the ratings of the goods and services will be, which in turn attracts new suppliers.

At present, however, sharing economy platforms are still some way away from occupying a dominant position in the market.¹⁶ As can be seen from the example of the established taxi industry, one of the two biggest companies – Uber – is actually breaking up protected structures that, through regulations and laws, had gained a competitive advantage over new entrants to the market.

Even if online intermediary platforms were in future to achieve a volume that could be problematic from the point of view of competition policy, the need for government intervention remains dubious for three reasons: Firstly, companies would have very little incentive to invest in new technologies and business models if government were to intervene every time these became too

big. As far as the competition authorities are concerned, therefore, a balance must always be struck between supporting competition and maintaining incentives for innovation.¹⁷ Secondly, market entry barriers in the sharing economy are relatively low and the dynamic is high. In other words, companies can quickly lose their position and be forced out by newer, more innovative players. Thirdly, customers can use other platforms or suppliers in the “traditional” economy, which also puts a limit on any concentration of power.¹⁸

Consequently, there is little justification at present for government intervention in the sharing economy on the basis of monopoly positions.¹⁹

Negative externalities

Market failure caused by negative externalities is a relatively frequent occurrence; one has simply to think of problems arising with transport or energy production. Obviously, therefore, the sharing economy may also be subject to various negative external effects. For example, car-sharing or the intermediation of car journeys leads to noise and pollution, the costs of which are borne not by the users themselves but by the general public. However, one could also argue that sharing models reduce traffic, and therefore ultimately reduce the negative effects of traffic. This is not necessarily so, however. In theory, falling costs and improved supply could see sharing models lead to greater congestion, if people use more transport services as a result.

Another example is noise pollution, which could arise as a result of the short-term letting of living space via online platforms. Guests who are only renting an apartment or a room for a few days are likely to be less interested in behaving appropriately towards their neighbours than long-term tenants.²⁰

Regardless of how extensive the negative externalities discussed might be, correcting such market failure through regulations specifically tailored to the sharing economy does not seem appropriate. The source of these negative external effects is to be found not in the sharing economy per se, but – in the case of the examples above – in the activity of car driving and the use of accommodation for overnight stays. So these negative externalities also arise in the “traditional” economy. If we want to reduce the negative effects, we must start with their origin. In the field of transport, a CO₂ tax might be appropriate, and in the field of accommodation provision, better solutions might include self-regulation or liability for damage.

The reverse case, where regulations to combat negative externalities only apply to “traditional” companies, even though they arise in just the same way in the sharing economy, is also problematic. An example of this might be safety regulations that apply in the taxi sector, and which are aimed at preventing accidents and concomitant negative consequences (damage to third parties). In New York City, for example, taxi drivers have to complete driving courses and undergo drug tests and medical examinations every year.²¹ In Switzerland, the regulations are less strict, but in most cantons taxi drivers are subject to mandatory traffic medicine monitoring. If the benefit of these regulations is greater than their cost, it makes economic sense to extend the regulations to the sharing economy. It should be noted, however, that many of these regulations can also be replaced by self-regulation. For example, rating and monitoring systems provide great incentives to drive carefully, since all information concerning each journey is digitally retrievable and any drivers who do not abide by the rules can be quickly identified.

11. Cf. footnote 4 on this point.

12. Results which are efficient from an overall economic viewpoint usually relate to the Pareto Optimum, which describes a state in which none of the market participants can be placed in a better position without others being placed in a worse position.

13. Brunetti 2013, Varian 2007.

14. This approach goes back to Stigler 1971, Posner 1974 and Niskanen 1971.

15. Brühn and Götz 2014.

16. Certify 2015.

17. Langenegger 2015.

18. Haucap 2015. Accordingly, in a recent decision in regard to Booking.com the Swiss Competition Commission WEKO was not able to establish beyond doubt that the behaviour of Booking.com represents a restriction of competition: decision of 19 October 2015 in the case of online booking platforms for hotels.

19. The same conclusion is also reached by Peitz and Schwalbe 2016.

20. Peltz and Schwalbe 2016.

21. Edelman and Geradin 2015.



Information asymmetries

Many of the areas where the sharing economy has gained a foothold are characterised by information asymmetries.²² Someone renting accommodation knows far less about the equipment, cleanliness and quality than the landlord. Such information asymmetries are particularly acute in the field of personal transport: a passenger is unlikely to know what qualifications a taxi driver has, or what his behaviour is like, or how clean his vehicle is. As mentioned previously, this can prevent better quality, safer products and services from becoming established in the market. The fewer customers there are for a given product, the more likely this situation becomes.

In order to reduce such information asymmetries, thereby improving quality and safety for consumers, the government

has introduced a wealth of regulations for both the hotel industry and the taxi industry. The example of the Canton of Zurich shows how detailed these regulations are: to operate a taxi firm, an operating licence is mandatory, and this is subject to certain requirements, such as the possession of a taxi ID, and not having had any offences reported in the last five years in connection with the exercise of one's profession in the taxi sector.²³ Similar regulations apply to taxi drivers: they must have a driver's licence that allows the transportation of persons on a professional basis, they must have adequate knowledge of the German language, and they must not have been guilty of repeated misconduct in the last five years. In addition, they must have passed a special test in which they are asked written questions about the addresses of dozens of locations such as hotels, hospitals, squares and streets (the local knowledge test). Regulations also apply to a number of other things such as maximum tariffs, drivers' behaviour, and vehicle cleanliness. The police department can also limit the number of operating permits, although this has not yet happened in the Canton of Zurich as it has in other Swiss cantons and towns.

Whether this multiplicity of regulations effectively increases the quality and safety of taxi journeys is questionable. Some of them have probably long since been superseded by technological advances. This is true, for example, in the case of the local knowledge test, which has become superfluous thanks to navigation devices and smartphone apps. Other regulations serve to protect taxi firms rather than consumers. According to a study by the George Mason University, the example of the taxi industry shows that regulations often create market entry barriers. In such situations, the regulators do not serve to correct market failure, but instead protect businesses from competition, or enable them to increase their earnings.²⁴ This is a form of "government failure". Although both quantitative restrictions on the supply of taxis and price-setting by the government are justified on grounds of consumer protection, the main effect is probably to protect suppliers. The Monopolies Commission in Germany, which has addressed taxi market regulation in a comprehensive report, argues for the removal of the limit on taxi licences and of the prescribed tariff, which is effectively a step towards deregulating the German taxi market.²⁵

On the other hand, regulations such as the background check on taxi drivers can serve a purpose, since they counterbalance information asymmetries and increase safety without leading to excessively high barriers to market entry or inspection costs. Although regulations on cleanliness or driver quality may be appropriate in theory, they often fail in practice. It is difficult to specify the cleanliness of taxis and the quality of drivers by law, or to carry out any effective monitoring. It is therefore hardly surprising that the poor quality and cleanliness of Swiss taxis repeatedly forms the subject of reports and policy proposals, despite a plethora of regulations.²⁶

The problem of asymmetric information can often be resolved without recourse to government regulations. Considerable progress in information technology has helped to rectify information asymmetries without government involvement. Online platforms are based on mutual rating systems that allow suppliers and customers to rate each other. As a result, the consumer has information about the supplier. Anyone wanting to hire out or sell his products and services on sharing economy platforms needs good ratings.²⁷

This creates a great incentive to behave in an exemplary fashion and to offer high-quality goods. In addition to rating systems, driving services intermediaries such as Uber offer monitoring systems that provide the consumer with further information. With GPS, the customer can see exactly where his taxi driver is. Ordering and paying by app means that the consumer can at any time digitally retrieve additional information such as the driver's name and rating, the vehicle registration number, and the fare amount. Platform operators themselves have a huge interest in safety and quality. It is therefore not surprising that driving services intermediaries such as Lyft carry out precise checks on each driver and withdraw them from circulation relatively quickly in the event of any misconduct. Compared to government, which must safeguard the rights of all parties in all proceedings, online platforms can implement such measures quickly and at no great cost.²⁸

Self-regulation can be found in all areas of the sharing economy and is at the heart of this business model. Without rating systems, there would be little transparency and trust, and the sharing economy would not enjoy its current success. Like driving services intermediaries, platforms for renting accommodation also include reciprocal rating systems, which provide the customer with information on the cleanliness and quality of the accommodation and the reliability of the provider.

However, self-regulation cannot solve all information problems, because rating systems can be incomplete or distorted. For example, distortion can arise if the experiences of customers who have not given a rating tend to be more negative.²⁹ It may therefore be desirable to have certain minimum standards specified by law, such as background checks and a duty of insurance for drivers operating in the sharing economy (background checks could be carried out by the platforms themselves, which already happens to a large extent).

22. Cohen & Sundararajan 2015.

23. Ordinance on the taxi industry in the City of Zurich 935.460.

24. Koopman et al. 2014.

25. Monopolkommission 2012/2013.

26. Gerny and Aschwanden 2013.

27. Of course the converse is also true – the driver can evaluate the customer.

28. Cohen and Sundararajan 2015.

29. Edelmann and Geradin 2015.

Are standard regulatory framework conditions necessary?

Overall, it is clear that the personal transport and accommodation sectors are affected by market failure, caused largely by information asymmetries. The most appropriate instruments for correcting this market failure are, firstly, rating and monitoring systems, which in contrast to government regulation do not lead to high market entry barriers or hinder competition; and, secondly, the application of certain minimum legal standards to complement self-regulation.

Sharing economy suppliers operate in a pre-existing economic structure and compete with “traditional” economy suppliers who are subject to significantly greater regulation than that postulated in the regulatory framework envisaged above. This raises the issue of whether the regulatory framework that currently applies to the “traditional” economy should also be applied to the sharing economy. Such a “level playing field” is what representatives of the affected sectors are asking for.³⁰ Specifically, they propose

that equal conditions should be created by transferring all existing regulations to the sharing economy.

This approach is hardly warranted, though. Firstly, technological progress has made many of the existing regulations obsolete (the local knowledge test for taxi drivers, for example), or the regulations have become barriers to competition (such as the quantitative limit on taxi firms). Instead of applying all existing regulations to both the traditional economy and the sharing economy, therefore, we should consider reducing the amount of regulation. The sharing economy provides an opportunity to do away with a regulatory system that has built up over time, and create a new regulatory framework.³¹

Secondly, a level playing field is not always desirable. On the contrary, the point is to achieve a correction of market failure. Because information asymmetries are largely removed in the sharing economy through self-regulation, fewer (or at least different) government regulations are needed to provide consumers with the same degree of protection that they have in the “traditional” economy.³² A tourist is unlikely to use the same taxi driver more than once, and is therefore unlikely to have information about the price and quality of the service provided or the reliability of the driver. The situation is quite different in the sharing economy: thanks to digital rating and monitoring systems, this information can be called up in advance and subsequent checks can be carried out on the services provided. An existing regulation may therefore be necessary in the “traditional” market but is not always necessary in regard to comparable services provided in the sharing economy.

Thirdly, there is the further consideration that the sharing economy largely consists of private suppliers. If you are only letting your apartment for a few days a year, for example, you should not be subject to the same fire safety regulations as a hotel.³³ The costs and benefits of such regulations would be disproportionate for private individuals. On this point, legislation could

define a practical threshold which would take into account the specific risks on the one hand and the rating and monitoring systems on the other hand, to satisfy existing legislative objectives. Unlike the present situation, such practical thresholds would no longer be based on the juristic definition of “business” activity. This distinction has become almost irrelevant, because it is hardly adequate to cover fragmented remunerated activity or a sharing economy.³⁴ By contrast, compliance with other regulations, such as collecting tourist taxes from apartment landlords, could be achieved quite easily by creating an interface with the intermediary platform. Airbnb already collects tourist taxes in several countries and cities and passes them on to the tax administration.³⁵

Sometimes opponents of the sharing economy also demand equal treatment for employed and self-employed persons. Taxi firms complain that they have to pay social security contributions for their employees, while such costs do not arise for Uber because the drivers are self-employed. From an economic standpoint, this argument does not hold water. Studies show that where employers are legally obliged to pay social insurance contributions, in the longer term these are mostly translated into lower wages for employees.³⁶ In other words, ultimately it makes no difference who has to pay these charges on paper. The distinction between entrepreneurs and self-employed persons makes little sense here, as long as the latter are also obliged to pay social security contributions.

It would be worth creating a digital tool that both employers and self-employed individuals could use to upload earnings from professional services, as has been suggested recently.³⁷ Standard rates could be levied for AHV [old age and survivors’ insurance], IV [disability insurance], ALV [unemployment insurance], BVG [occupational pension] and accident insurance, so that everyone would be treated equally. The distinction between the employed and self-employed would become obsolete.

The sharing economy from a legal perspective

The two functions of the law

How, then, are the economic characteristics of the sharing economy to be implemented in law so that full use can be made of the economic opportunities presented and at the same time the regulatory purposes envisaged in the legislation are safeguarded?

In today’s economy, the law has to fulfil two functions. Firstly, it has to regulate the legal relationships between market participants, securing their expectations and thus reducing transaction costs. Private law provides market participants with institutions such as “ownership” and “possession” for this purpose, as well as various contractual and corporate forms. On the other hand, economic law is also responsible for regulation. Rules are embodied in law that pursue political and social purposes. This type of regulation is primarily to be found in public law, but also occasionally in private law. Somewhere in between is the law of digital communication, which is regulated by several areas of the law.

Safeguarding expectations and social contract law

In principle, private law is characterised by its considerable flexibility. Based on the principle of freedom of contract (Art. 19 (1) of the Swiss Law of Obligations [OR]), the parties can define their own rules for their transactions. Where such rules have not been defined, the Law of Obligations provides a wealth of regulations to determine contractual content, based on the principle of safeguarding expectations. The civil courts (and in the final instance the Federal Supreme Court) apply contract law in the context of specific cases of dispute, and develop the law as necessary. In this context of freedom of contract, statutory norms based on the safeguarding

of expectations, and the development of the law by the courts on a case by case basis, contract law can reliably and dynamically adapt to new requirements. The same will be true in the context of the sharing economy.

On the other hand, the social norms of contract law are a cause for concern: if the parties specify contractual content, then (depending on the type of contract) mandatory norms also determine the contractual content, i.e. norms from which the parties cannot deviate. In particular, legislation provides corresponding social law for the protection of employees and tenants and (more recently) consumers. However, the participants in the sharing economy cannot always be classified into these dichotomies of strong/weak or commercial/private which form the basis of present-day mandatory contract law, and the economic purposes of the regulation which have been described above tend to disappear from view. The following current problems serve as examples of this:

In the context of intermediation activity in regard to accommodation, the question arises as to whether and to what extent the social protection mechanisms of the law of tenancy apply – on the one hand in favour of the main tenant who is subcontracting his dwelling, and on the other hand in favour of the subtenant.³⁸ The main lessor can – as a consequence of social tenancy law – only prohibit his main tenant from subletting under certain conditions, specifically if no “significant” disadvantages arise for the lessor, and if the subletting conditions are not abusive by comparison with the conditions of the main tenancy (Art. 262 (2) OR). This limits the freedom of contract of the lessor, whose property could, as a result of being offered via an Internet platform, be used



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30. See footnote 4 on this point.

31. See Avenir Suisse 2016 on this point.

32. Sinclair 2016.

33. According to a Walliser Tourismus Observatorium study, 5% of lessors on Airbnb look after more than two properties, and are therefore to be classified as commercial lessors. Cf Walliser Tourismus Observatorium 2015.

34. Cf. footnote 51 below on this point.

35. The complete list can be found here: <https://www.airbnb.com/help/article/653/in-what-areas-is-occupancy-tax-collection-and-remittance-by-airbnb-available>.

36. Melguizo and Gonzalez-Paramo 2012.

37. Bütler 2016.

38. Jud and Steiger 2014; Spirig 2015.



to a considerably greater extent than he would wish, while it is possible that the main tenant does not even occupy the property himself. But the main tenant's freedom of legal arrangement is also considerably restricted by mandatory tenancy law: case law to date (which has not focused on the sharing economy) requires that any sub tenancy rent may not be more than 3% higher than the main

rent. The question also arises as to whether the user of an Airbnb service can demand an extension of the subletting relationship if the termination of the tenancy would result in hardship for himself or his family (Art. 272 OR), or if indeed he can demand a reduction in an excessively high rent (Art. 270 OR). The courts will have to judge whether these rules of social contract law can be automatically applied to the sharing economy. Correctly, the courts will take into account the fact that the dichotomies that in social private law are presumed to exist do not normally apply in the sharing economy in the same way as they are presumed to apply in the statutory regulations, and that consequently the justification for a regulation can be superseded by new economic realities. Accommodation that is arranged via Internet platforms may possibly have to be classified not as a sub-tenancy, but as a new kind of contractual form (an "innominate contract") containing both

tenancy agreement and order contract elements. This would provide some freedom for the courts to determine the applicability of current social law on the basis of specific cases, and for the parties to regulate their sharing economy transactions themselves.

The question of the application of social law is also a feature of the debate concerning intermediation platforms for driver services. Discussions are currently taking place in several countries as to whether Uber does in fact only act as an intermediary for "sharing" services, or whether an employment contract arises between Uber and Uber drivers, as the Labor Commission in California decided in the case of *Uber v. Berwick* (2015). In Switzerland also, this question is the subject of heated debate.³⁹ Ultimately the courts will have to decide the matter, and thus define when the mandatory protection standards of labour law and

social insurance law have to be taken into account. On the one hand it is obvious that not everyone who offers their sharing services via Internet platforms needs the protection provided by labour law. On the other hand, it has become standard practice over the last hundred or so years for specific social rights (in particular, termination notice periods, continued payment of wages in the event of sickness, and social insurance) to be granted to persons who are integrated into the operation of their work-provider and who are subject to their work-provider's directions and instructions.⁴⁰ Here too it will be for the civil courts, on the basis of specific cases, to draw an appropriate line of separation between social private law and freedom of contract which will take into account the protection desired by the legislation, on the one hand, and the economic concerns of the sharing economy on the other hand. The more the platform operators restrict their users'

freedom of legal arrangement in business, and the more the living requirements of the users become dependent on the platform and the decisions of the platform operators, the more the courts are likely to regard such arrangements as employment contracts and the more the parties will have to operate according to social contract law – and bear the economic costs thereof. In reference to the existing sharing platforms and on the basis of labour case law to date, however, it is highly unlikely that employment contracts will be deemed to exist, particularly as those offering sharing services do not usually make their living solely from a sharing platform, and the sharing platform operators will impose limits on themselves, particularly in light of the threat posed by labour law.⁴¹ However, the social issue will not disappear, particularly in light of the increasing fragmentation of earned income that has been identified.⁴² A minimal and easy-to-manage protection of livelihood,

specified in legislation, which would cover both typical social insurance risks and (by analogy with protection from dismissal for employees) the risk of a sudden and substantial reduction in order volume or income, for example in the event of a change in the conditions of intermediation or exclusion from a platform,⁴³ would in this situation be preferable to any over-hasty extension of social contract law.

39. Cf. Sommer 2015 and NZZ am Sonntag of 8 May 2016, „Das Uber-Modell ist nicht AHV-tauglich“ [the Uber model is not suitable for old age and survivors' insurance, with references to decisions of SUVA and SVA Zürich, which classify Uber as an employer. More recently, NZZ of 30 August 2016 with reference to the Pärli report commissioned by the trade union Unia.

40. Cf. Federal Supreme Court decision 4C.220/2003 cons. 2 on the case of a lorry driver.

41. Similar view in Lingemann and Otte 2015 in regard to German law.

42. Singer 2014; Das Acevedo 2016.

43. The situation is similar in regard to the USA: Harris and Krueger 2015. However, social security in the USA is probably generally much poorer than in Switzerland.



Digital communication and the right of self-regulation

In the sharing economy, digital communication is just as important as it is in other digital forms of business. The regulation of digital communication by means of the norms contained in data protection law, copyright law and the right of personality does not therefore require any detailed explanation here.

It should however be emphasised that with the evaluation and monitoring systems the digital platforms have created a separate, non-juristic self-regulation which is however in turn subject to legal restrictions such as those envisaged in data protection, the protection of personality, copyright, the rules against unfair competition, and criminal law.

Two problems in particular seem to stand out in the context of sharing platforms: firstly, the exclusion or non-admission of users, and secondly the importance of self-regulation.

If the platform operator really does not have to accept any responsibility whatsoever for the observance of existing regulations and social standards, it could encourage the service suppliers to extend their sharing activities without any concern as to whether these suppliers fulfil the regulatory standards of (say) the taxi industry or the hotel industry. If the service providers were fined because of a violation of regulatory standards, the platform operator could exclude them from its sharing platform in order to avoid coming into conflict with the authorities. Such practices would be dubious, and any such exclusion (and also non-admission) could be challenged by appealing to personality rights⁴⁴ and the obligation

to enter into a contract as established by the Federal Supreme Court.⁴⁵

As has been shown, the self-regulation of the sharing platforms to some extent achieves the same effects as have been achieved up to now by statutory regulation. It is open to debate whether the statutory regulation is actually still necessary and therefore legally valid.⁴⁶ The question of whether the effect of self-regulation is to render state regulation obsolete is however only one consideration. We must also ask whether self-regulation has sufficient legitimacy to replace state regulation.⁴⁷ This is not a new topic. As long ago as 2008 the then Swiss Federal Banking Commission (now FINMA) required that in the context of the enactment of self-regulation or any amendment thereto the central concerns of the state legislation process must be appropriately reflected, such as in particular transparency and the right of the persons concerned to a fair hearing.⁴⁸ Today this is (still) not a legal requirement for valid self-regulation, since self-regulation (as part of private law) in principle profits from the freedom of contract. However, its legitimacy vis-à-vis those who are directly affected by self-regulation is an indication that legislation should withdraw its statutory regulation in favour of private regulation.

Public law regulation

The above mentioned social law of contract, by which parts of the content of a contract are specified in the legislation on a social and political basis, represents the smaller part of state regulation of the economy. Of greater significance are those norms of public law by which the state places an obligation upon those who are subject to its law to take action or refrain from an action, in order to avoid danger, or with certain social goals in mind, or for the purpose of state financing.

In our highly dynamic economy, however, such social engineering is usually implemented "blind", i.e. without any precise knowledge of the unintended consequences that can often occur. For this reason it is now generally acknowledged that legislation should always base its regulations on as precise a knowledge as possible (both qualitatively and quantitatively) of the subject of regulation, and that the consequences of regulation should be monitored so that any necessary corrections can be made.

In principle, the goods and services offered within the sharing economy are protected by our constitutionally guaranteed economic freedom. This freedom guarantees free choice of profession and free access to any gainful activity in the

private economy, and the free exercise of such activity (Art. 27 of the Federal Constitution [BV]). State regulations that restrict the goods and services of the sharing economy, therefore, ought not in principle to be directed against the competition. In addition they must have a legal basis, they must be justified by public interests, and they must be proportionate (Art. 36 BV).

According to the Federal Supreme Court, economic policy regulations, i.e. in particular measures that secure or favour certain branches of industry or certain management forms, are anti-competitive and therefore inadmissible. By contrast, regulations that pursue law enforcement purposes or social policy purposes (e.g. accident prevention or consumer protection in the taxi industry) are permissible. It is important to take into account not only the motives behind the regulation but also its effects. Particularly in the case of the taxi industry, the Federal Supreme Court has repeatedly made it clear that regulations that are detrimental to price competition must serve a permissible and clearly proven public interest. In particular, the obligation to be in contact with a radio headquarters, minimum prices and territorial delimitations would fail to meet this criterion.⁴⁹

44. Art. 28 of the Swiss Civil Code [ZGB], cf BGE 86 II 365 in regard to the so called boycott ban.

45. BGE 129 III 35 An obligation to enter into a contract applies in the context of 1) "goods that are needed for daily life", which 2) are publicly offered and 3) for which there is no alternative, if 4) no legitimate reasons apply for refusing to conclude a contract.

46. See Public-law regulation below on this point.

47. This is not to be confused with the rating and monitoring systems whose purpose is the transparency of the services being traded. These are however rules that form the basis of the sharing platform.

48. EBK-Bericht Selbstregulierung 2007.

49. BGE 121 I 129; Supreme Federal Court decision 2C_940/2010. Cf most recently Supreme Federal Court decision 2C_547/2015 on Uber in Geneva

Regulations that have the effect of putting the sharing economy at a disadvantage, or even excluding it from the market, ought therefore to be viewed with a critical eye. This relates above all to regulations which are too hasty in classifying a provider as “commercial” and which stifle that provider under a vast quantity of regulations.⁵⁰ Instead, in regard to the sharing economy the separation of “commercial” and “private” should be fundamentally rethought, because the sharing economy usually does not fit these categories.⁵¹ The direct connecting point for a regulation must then be the question of whether market failure has occurred in certain situations, i.e. whether there are any negative effects or information asymmetries. For example Uber, by making it possible for a car driver to transport other persons, is (as the intermediary) creating a risk potential. It should therefore be responsible – in accordance with the risk potential that has been created – for undertaking reasonable checks on the suitability of the driver. Neither should the commercial aspect, i.e. the planned achievement of profit, be the deciding factor as to whether a person is subject to hotel industry regulations. On the contrary, the deciding factor should be the risk potential that has been created, i.e. it should (for example) be the number of overnight stays. In addition, in the case of electronic intermediation platforms the traditional information asymmetry between the taxi driver and the passenger typically no longer exists, so that the duty to “affix a taximeter in a clearly visible place”⁵² is open to question. The point of connection here should be the information asymmetry, not the commercial nature of the activity.

Above all, previous regulations which were oriented to the specific needs of the “offline economy” ought not to be automatically

applied to the sharing economy. For example, previous regulations may well have been necessary to compensate for information asymmetries which were disadvantageous for taxi customers, and to protect taxi customers from any unnecessary detours taken by the driver. If the sharing economy produces services that take account of legislative concerns by other means, the regulation is no longer necessary and therefore loses its legitimacy.

Economic freedom also requires that competitors should be treated in the same way. However, this can present problems in terms of regulation, because although the goods and services offered in the sharing economy are directed at the same public as previous “offline” goods and services, and they satisfy the same consumer needs, nevertheless the sharing economy follows different economic rules.

The question of whether the previous regulations for the offline world can indeed be made to fit the sharing economy, and whether they have any legitimacy in law, has to date been almost ignored in the legislation. To some extent this is logical, since new economic phenomena should first of all be observed, and any regulation should only be issued on the basis of well-founded knowledge. It is however problematic that this discussion is being led not by the law makers but by the state administration and the law enforcement authorities, who seek to enforce the existing regulatory standards on the “little people” (i.e. the service providers), in particular by using the means provided by criminal law. Criminal law, actually the *ultima ratio* of the law, is thus being used for an alien purpose, and the burden of the discussion on regulation generally falls on those who are trying to make a living in the new sharing market.

50. Jud and Steiger 2014.

51. Kreczer-Levy 2015.

52. Art. 10 (1) of the Taxi Regulations of the City of Zurich.



Conclusions

From an economic point of view, regulations can be particularly useful if the market is not producing efficient results for the economy as a whole, a situation that economists refer to as “market failure”. If such a situation exists, government can try to increase social welfare by means of market intervention. However, because the political process is also liable to failure, new regulations do not always lead to a more efficient result.

In the accommodation and personal transport sectors, market failure can arise as a result of information asymmetries in particular. A person who rents accommodation knows much less about its equipment, cleanliness and quality than the lessor. Market failure can also be caused by negative externalities, for example if a taxi driver causes an accident and thereby also causes suffering to the customer or other persons. With the aim of eliminating such information asymmetries and avoiding negative externalities, government has introduced a plethora of regulations in the taxi industry and the hotel sector. Nevertheless it is doubtful whether these regulations always increase the quality of the service and the safety of the consumer, or whether they are actually (still) necessary. Some have surely long since been rendered obsolete by technological progress, while others mainly result in market foreclosure.

In the sharing economy, many of these problems can be solved without any government action, often with significantly greater efficiency. Two-way rating systems provide information not just about the

quality of the product (e.g. the equipment and cleanliness of the accommodation offered), but also about the reliability of the exchange partner (for example the driving skills and the pleasantness of a driver). As a result, rating systems not only eliminate information asymmetries but also create strong incentives for exemplary behaviour, which reduces the likelihood of negative externalities. In addition to rating systems, driving services intermediaries such as Uber offer monitoring systems which provide consumers with further information: with GPS, the customer can see exactly where his taxi driver is, and with payment by app, names and registration numbers can be retrieved at any time. Thanks to this form of self-regulation, ultimately fewer state regulations are needed to provide consumers with the same or even better protection that they would have in the “traditional” economy.

From a legal point of view, it is problematic that the sharing economy subverts important existing dichotomies of social regulation, such as “strong/weak” and “commercial/private”. Social private law, particularly where it aims to protect tenants and employees, cannot properly get to grips with the new parameters present in the sharing economy. Any over-hasty transfer of mandatory norms which were originally intended to deal with very different problems could hinder the development of new kinds of welfare gains through the sharing economy. For this reason the parties should on the one hand be given the opportunity (by application of the principle of freedom of contract) to define appropriate rules for the sharing

economy themselves. In cases of dispute it will be for the civil courts to determine, on the basis of specific cases, how far our present social law should apply. On the other hand the legislation should ensure a minimal and easily workable securing of livelihoods which will also cover the typical social insurance risks faced by people working in the sharing economy.

So far, platform operators have regarded the regulation of access to their intermediation services (and also the regulation of the associated monitoring and rating systems) as their own concern, and they reserve the right to amend the corresponding regulations at any time. However, exclusions (or non admittance) can be challenged in court, particularly on the basis of personal rights and the private-law obligation to enter into a contract. In addition it should be required that the self-regulation of the intermediation platforms (by analogy with self-regulation in the financial market) must acquire legitimacy through transparency and the right of the parties concerned to a fair hearing.

Previous public-law regulation which was aimed at “offline” sectors ought not to be automatically applied to the sharing economy. In particular, regulations that have the effect of putting the sharing economy at a disadvantage, or even excluding it from the market, could be inadmissible in light of the practice of the Federal Supreme Court to date. This applies also in regard to regulations that are no longer necessary because the sharing economy takes account of legislative concerns by other means.

As far as the legislation is concerned, therefore, the following six measures need to be addressed. Taken together, they form a kind of regulatory framework for correcting market failure, easing the burden on the traditional economy, and ensuring the necessary legal safety:



Regulations in the “traditional” economy which have grown up historically and are no longer relevant should be abandoned. Examples of this are the local knowledge test for taxi drivers and the quantitative restrictions on taxi firms.



Rating and monitoring systems, as a form of self-regulation, should be accorded statutory legitimacy. Such systems are capable of replacing many of the traditional regulations and achieving the same aims more efficiently.



Because self-regulation cannot solve all problems, certain minimum state requirements should also apply to sharing economy platforms, such as the background check for drivers and the duty of registration for foreign tourists staying overnight.



Since the legal distinction between “commercial” and “private” is almost impossible to apply to the sharing economy, proven aspects of market failure and in particular specific hazard situations should form the starting points for minimum requirements. For example, the requirement that (electronic and traditional) driving services intermediaries must carry out a background check on their drivers should not depend on whether or not the activity is “commercial”, but should – in accordance with the risk potential – apply generally. In the accommodation sector, certain minimum standards could depend on the number of days the property in question is let. The effectiveness of the regulations should be periodically reviewed and corrected if necessary.



Through a cooperation between the authorities and platform operators, taxes such as visitors’ tax could be collected at no great administrative cost.



A similar solution should also be aimed for with regard to the social security envisaged for the working population: with the aid of a digital tool, contribution rate billing for social security is easily achievable, not only for businesses but also for individuals or intermediation platforms. The distinction between the employed and the self-employed would no longer be of prime importance.

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