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The Sharing Economy Has Landed

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One of the highest grossing movies of late 2006 was a romantic comedy, *The Holiday*, starring Cameron Diaz and Kate Winslet. In the film, the two women visit a home-exchange website and agree to swap their homes in England and Los Angeles for two weeks over Christmas. Happily, they each find romance during their time in the other person's house.

Part of the success of *The Holiday* was due to the premise of using the internet to access distant, desirable real estate. In the eleven years since *The Holiday* was released, the use of the internet for all types of real estate transactions has not only increased dramatically, it also has evolved. Today, there are hundreds of websites that are online advertising spaces; enabling individuals and businesses to find seemingly limitless listings of traditional real estate assets such as vacant space in office buildings, malls and strip centers, homes for sale, and available hotel rooms. However, applying the internet to real estate also has resulted in a new class of real estate transactions: access to underutilized real estate.

The internet now enables real estate owners to turn unused or underutilized portions of their real estate into revenue generators. Via the internet, owners can find users for their extra bedrooms, open shopping mall areas, or excess office space. The internet now allows individuals to optimize their real estate assets by finding uses for any excess capacity.

This phenomenon is commonly referred to as being part of the "sharing economy." Technological growth has made data about shared real estate assets more available (businesses and individuals can easily find available excess space), and technological advances have reduced transaction costs of sharing those assets (think PayPal and other direct payment apps). The end result is that it is now "worth it" to disaggregate real estate and find users for the underutilized portions.

Today, nearly every sector of real estate is a part of the sharing economy. This article will explore some of the forms the sharing economy has taken to date in residential, office and retail real estate and analyze some of the constraints that affect these innovations and may limit their future growth.

AIRBNB

One of the best-known applications of the sharing economy to real estate is Airbnb. Airbnb began in San Francisco in 2007, when roommates Brian Chensky and Joe Gebbia decided to rent out space on an air mattress in their apartment. In 10 years, it has grown to be the dominant online marketplace for people to rent out their homes, extra bedrooms, apartments or other accommodations to provide short-term lodging. Industry estimates are that in 2017, over 100 million short-term apartment and room rentals were booked through Airbnb. *Bloomberg* reported that Airbnb made its first profit in the second half of 2016 and there are indications that Airbnb has maintained its profitability for 17 months. *Fortune* has stated that by 2020, Airbnb›s earnings before interest, taxes and depreciation may be as high as $3.5 billion.

RETAIL SPACE

While it is not as widely known as Airbnb, the use of the internet to access excess retail space is quickly growing. Spaces available by the day, week or month can be viewed and booked using a number of websites. Two online marketplaces for short-term retail space are Appear Here and Storefront.

Appear Here is a UK company founded in 2013 by then 20-year-old Ross Bailey. Appear Here provides an online marketplace for short-term retail space in London, Paris and New York. According to the Appear Here website, the company is more than a listing service, providing personal treatment to tenants to match them with spaces that are coordinated with their particular brand and providing landlords with real-time information on rents and demand. Examples of the retail space available on its website include a 350 sq. ft. boutique in the Nolita section of New York City for $560/day, a 40 sq. meter showroom in the Le Marais section of Paris for 270 Euros/day and a 400 sq. ft. shop in Covent Garden in London for 392 Pounds/day. Very interestingly, Appear Here claims that it regularly books space in less than 3 to 6 days.

Storefront was started through a start-up accelerator by Erik Eliason and Tristan Pollock in San Francisco in 2012. Its listings are short-term rentals of temporary vacancies. Current space availability on its website includes locations in London, Paris, New York, Los Angeles, San Francisco, Hong Kong, Amsterdam and Milan. Storefront states that the average time to book space using its platform is 12 days, as opposed to a 60 day average time to set up a traditional retail store.

In addition to listing temporarily available space online, some retail landlords are now using the internet to market "permanent temporarily available space." Retail landlords, seeing some excess space in their traditional on-line stores, are turning those locations into "Permanent Pop Up" venues. Once upon a time, retail landlords marketed their vacant space for a "pop Up" location until a longer-term tenant was found to occupy the space. However, retail landlords are now recognizing the huge number of companies that only want to rent space on a very short-term basis, generally six weeks or less. The January 2018 edition of *Shopping Centers Today* highlights the efforts of Simon, Washington Prime Group and Westfield Corp. to market space to e-commerce and other up and coming retailers. The space is offered on a short-term basis, giving the tenants a low-risk point of entry into the brick-and-mortar world, and providing landlords with a steady stream of new customers.

OFFICE SPACE

While the lodging and retails sectors are growing areas of the sharing economy, the most economically successful example of real estate in the sharing economy is coworking office space. In 2005, the first official "coworking" space was opened by programmer Brad Neuberg in San Francisco. His original flyer promoted "Coworking: Community Office Space for Writers and Programmers" as an alternative to "working from coffee shops every day" which would provide community and structure. Brad's coworking space was limited to five total members! Since those humble beginnings, studies have shown that the number of coworking spaces has approximately doubled each year, and current estimates are that over 1 million people worldwide are working in coworking spaces. These shared workspaces can be extremely flexible. Rental agreements can range from a number of days, to a month or a much longer term. Space can accommodate one individual or a company with more than 1,000 employees.

The dominance of shared workspaces may be best exemplified by the late 2017 sale of the iconic Lord & Taylor department store on Fifth Avenue in Manhattan reportedly to WeWork, a leading provider of shared workspace. WeWork was founded in 2010, has a valuation in excess of $20 billion, and is among Manhattan's largest office tenants. It has been reported that after the 2018 Christmas Season, Lord& Taylor will occupy only the bottom floors of the building, while the remainder of the building will be transformed into WeWork's headquarters.

OTHER APPLICATIONS

The internet and smartphone apps are enabling individuals to rent out almost any available space. Current websites provide amazing examples. You need a parking spot … I have space in my driveway or garage. You are looking for short term storage … a portion of my attic is available. You are searching for a convenient workspace; my dining room is available every morning for up to 5 people and coffee and muffins are in the adjoining kitchen!

While all of these examples demonstrate the tremendous growth of real estate in the sharing economy, there are some factors that could limit continued expansion.

REGULATION

Real estate is one of the most highly regulated areas of any economy. Zoning use regulations, health codes, and operational licenses are requirements for almost any public use of real estate, and with good reason. Zoning regulations help ensure that residential areas, for example, remain free of commercial enterprises and that office buildings have enough parking for all occupants. Who among us would like to find out that the 3-bedroom house next door on our quiet street has turned into a small motel, with new guests arriving daily and an absentee owner or that the office suite next to us now has double the number of occupants using the building common spaces and parking lot? Health codes result in public accommodations being inspected and are designed to be sure that infestations don't occur, that facilities are cleaned and that building and safety regulations are satisfied. If establishments are less regulated, might fewer owners comply with these requirements? Licensing ensures that revenues are appropriately taxed and that facilities comply with wage requirements and non-discrimination laws.

For these reasons, many municipalities have pushed back on some aspects of the shared economy. In October 2016, New York State passed a law that fines owners who advertise the availability of their properties in violation of short-term rental laws. Pre-2016 New York law already prohibited the rental of an apartment in a three-or-more dwelling building for less than 30 days unless a "permanent resident" was present. The 2016 law was in response to a 2014 New York Attorney General report on the increase in using "traditional apartments as transient hotel rooms" due to the rise of short-term rental platforms. The new law imposed fines of $1,000 for the first violation, $5,000 for the second violation and $7,500 for each successive violation, making it illegal to rent an apartment or entire home on Airbnb or a similar platform for less than 30 days unless the host is present. Airbnb immediately filed suit to enjoin the enforcement of the law, and within the next two months, both New York State and New York City entered into settlement agreements with Airbnb, agreeing not to enforce the law. More recently, in January 2018, legislation was introduced in the New York Legislature allowing short-term rentals of a single home, while requiring hosts to carry $250,000 of insurance and allowing the listing companies to collect and remit taxes.

Similarly, Boston Mayor Marty Walsh said in January 2018 that he is filing a proposed city ordinance to require short-term rental operators to register with the city, pay an annual fee and limit the number of nights that a unit can be rented in any year. The ordinance also would require Airbnb and other online marketplaces to provide Boston with data on rentals.

LEASES AND OTHER PRIVATE RESTRICTIONS

In addition to complying with statutes and regulations, and obtaining all needed licenses, the use of real estate often is subject to a variety of private restrictions. Some of these restrictions appear in leases, condominium declarations or home owner association documents and can directly affect the use of real estate by short term users.

Retail shopping malls, shopping centers and office buildings all have a number of leases which must work in tandem. Use restrictions and sharing of common areas and operational expenses are but three examples of typical private requirements placed on tenants. Will landlords apply use restrictions to a user who is only renting for 4-6 weeks? Will "Pop-Up" tenants be charged a share of taxes, insurance and operating expenses? Should coworking offices pay a higher share of operating expenses on the assumption that there are more people per square foot in their locations? Is it worth complaining to the landlord? If a long-term tenant complains about a short-term user, the short-timer may be gone before any action can be brought against the landlord!

The use of units in a condominium or homes in an HOA also can be subject to long documents, which specify extensive penalties for a breach. However, who is going to monitor websites to see if the "guests" your neighbor has on a regular basis are her relatives from across the United States or are customers who found her on the internet? Are there enough guest parking spaces for everyone "visiting"? Why are there suddenly no open chairs at the pool on the weekend?

FUTURE

The sharing economy is here to stay, and innovators will continue to find more ways to maximize the use of real estate by offering the use of discrete aspects on the internet. Existing regulations and restrictions were not designed to address this phenomenon. However, the demand is too great, and the economic incentives are too strong, to allow constraints to prevent continued growth. Instead, regulations and restrictions will need to be modified to permit some level of shared use, while also protecting health, safety and tax concerns.

Mark Twain once said, "Buy land, they're not making it anymore." He didn't realize that the internet will continue to optimize the use of the land we have!

This article first appeared in Westlaw's publication entitled Sharing Economy. The publication is part of the Emerging Areas of Practice Series – a new publishing initiative which reduces product to market time to cover emerging areas of the law as they develop. New documents are loaded to Westlaw on a rolling basis as received and content is updated quarterly.

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