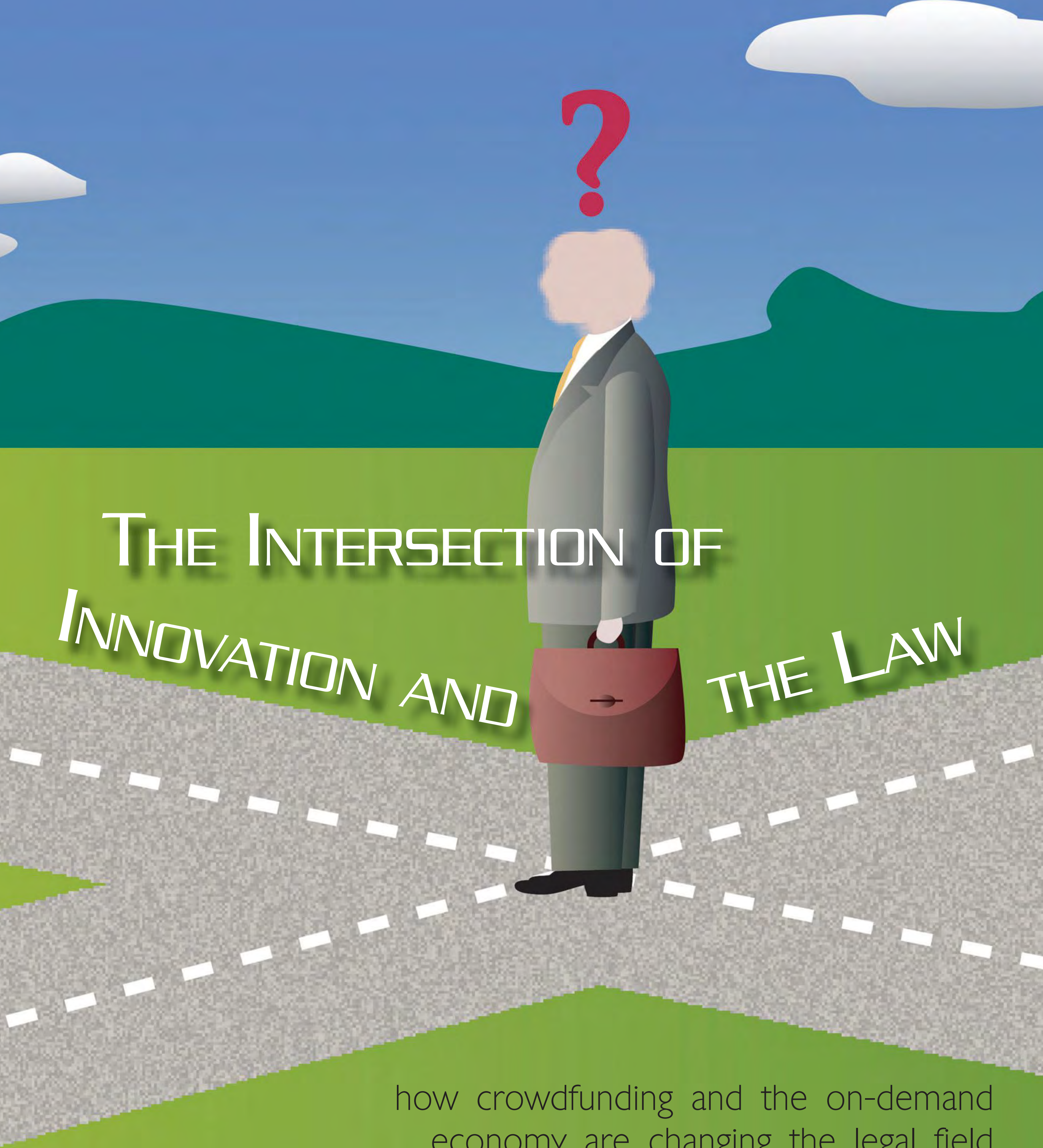
More than ever before, business and technological innovations are rapidly shaping the legal industry. Creating additional legal work for attorneys, innovative ideas bring about novel legal issues and require new interpretations and applications of existing law. As business models transform, laws and regulations must continue to evolve to address these novel issues. We, as lawyers, must be prepared to respond rapidly to emerging legal issues.



The Intersection of Innovation and the Law

how crowdfunding and the on-demand economy are changing the legal field

by Lucas E. Buckley,
Jesse K. Fishman
and Matthew D. Kaufmann

Innovative ideas disrupt the traditional or expected. In turn, these ideas are prone to generate litigation, and pioneering entrepreneurs often have an uneasy relationship with the law.[1] The correlation between innovation and litigation may relate to a number of factors:

1. Many innovative companies are using technology to invade highly-regulated industries;[2]
2. Innovators often apply the strategy of do first, seek forgiveness later;[3] and
3. Disruption often requires removing what is thought to be an essential component of an industry.[4]

Attacking highly regulated industries, acting without permission, and tweaking essential components may be helpful strategies for creating a competitive edge and revolutionizing an industry. However, these same factors are – not surprisingly – magnets for litigation.

The recent phenomena of on-demand and crowdfunding businesses are using technology to revolutionize the processes of purchasing and investing. Popular on-demand and crowdfunding companies have frequently made headlines due to their involvement in litigation. Just as these disruptive ideas create new business models, they also create new legal issues. This article examines the relatively new crowdfunding and on-demand businesses to demonstrate how we, as attorneys, must navigate the rapidly changing landscape created by innovation.

The On-Demand Economy

Business Models are Changing to Make Purchasing Faster and Simpler

Consumer behavior is changing.[5] The smartphone revolution "has made convenience, efficiency, and simplicity crucial ingredients in purchasing decisions."[6] As one observer puts it:

> Immediate access to messaging, e-mail, media, and other online functionality through smartphones has generated a sense of entitlement to fast, simple, and efficient experiences.[7]

Speed and convenience are now large factors in purchasing decisions because:

> The internet makes human desires more easily attainable. In other words, it offers convenience. Convenience on the internet is basically achieved by two things: speed, and cognitive ease. If you study what the really big things on the internet are, you realize they are masters at making things fast and not making people think.[8]

The on-demand economy – defined as "the economic activity created by technology companies that fulfill consumer demand via the immediate provisioning of goods and services" – responds to these consumer demands.[9] On-demand businesses like Uber, Lyft, GrubHub, and Instacart[10] are revolutionizing commercial behavior by using technology, often via phone apps, to immediately link the consumer to a good or service.[11] Uber and Airbnb have created a truly massive marketplace by:

> [S]implifying an existing process and providing an easy customer interface. Before Uber, you could get a taxi or car service and before Airbnb you could rent a property. It was just much more complicated for both the property owner and the renter, especially if the property was in a more obscure location. . . . [These companies] have taken the friction out, and created true marketplaces.[12]

These companies reduce costs by using lean models for labor – all they need to operate "are people with smartphones and cars" – while leveraging technology and using existing infrastructure.[13] In addition, on-demand companies can save up to 40% by classifying their workers as independent contractors rather than employees.[14]

This model has quickly made its mark. Venture capitalists have poured more than $9.4 billion into on-demand companies since 2010.[15] Uber has had so profound an impact that it has been compared to Google:

> Technology innovation is always spawning new words, but it is rare that the name of a company becomes a verb. Google is clearly the most prominent example of this phenomena, but now it seems, at least in the business world, that Uber may be becoming a verb meaning to 'radically disrupt' an entire industry.
> . . .
> The new breed of disruptive companies are the fastest growing in history.[16]

One commentator claims the on-demand economy "will represent the fastest and most significant shift in spending since the advent of internet commerce."[17] The on-demand revolution is here to stay.

How Innovation Affects Existing Models

Although innovation creates a competitive edge – through novel concepts and reduced costs – it also negatively affects existing models, creating conflicts in the disrupted industries.

In the on-demand economy, a primary conflict is in determining what laws and regulations apply. Ride-sharing platforms such as Uber and Lyft frequently face opposition from regulators and transportation lobbies due to the strict regulations placed on existing taxi services versus the open field on which Uber and Lyft seem to operate.[18] Traditional cab drivers complain of the competition, specifically that on-demand companies siphon off customers in lucrative markets while ignoring safety, quality assurance, and permitting regulations that govern how traditional cabs operate.[19] Another area of dispute is over "surge" pricing – where riders may be charged a premium for busy times of day – and the methods by which ride sharing drivers can flout the rules in order to secure a fare.[20] To avoid regulations that apply to traditional taxi companies, Uber argues that it is not a taxi company, rather that it is a platform connecting people who need rides to those who are willing to give them.[21] Cities around the world are banning Uber and ride-hailing apps because of their lack of safety measures and unfair competition.[22]

Another question for on-demand companies is that of liability. Uber drivers have been involved in shootings and car accidents.[23] If ride-sharing platforms are merely platforms rather than taxi services, another legal question arises: who is responsible when something goes wrong?[24] Ride-sharing platforms seem to be acknowledging some responsibility to put safe drivers on the road as they require certain levels of licensing and insurance and offer training sessions for their drivers.[25] However, the issue of training strikes another hot issue: are their workers employees or independent contractors? And, if the workers are independent contractors, to what extent can the companies they work for provide them with training and control their conduct?

The issue of whether to classify workers as employees or independent contractors has been heavily debated and litigated.[26] A recent decision of the California Labor Commissioner's Office fuels the long-simmering debate of classifying workers, stating that an Uber driver should be classified as an employee, not an independent contractor as was Uber's normal practice.[27] The California decision will not immediately revolutionize classification of workers in the on-demand industry because the decision does not apply beyond that particular employee, the decision may be overturned on appeal, and because Uber has prevailed in numerous states in keeping its definition of drivers as independent contractors.[28] Nonetheless, the California decision is important because it analyzes critical elements of distinguishing between employees and independent contractors, such as:

- The amount of control the company has over the work;
- Whether workers are engaged in work that is distinct from, or an integral part of, the work of the company; and
- The extent to which the company maintains quality control such as asking customers to provide feedback.[29]

In the weeks following the California decision, Instacart (a delivery grocery startup) and Shyp (a shipping services company) decided to reclassify some of their workers as employees.[30] A number of on-demand companies saw this coming and already moved to reclassify workers or counted their workers as employees all along.[31] In any event, the debate on worker classification is unlikely to end anytime soon.

Like ride-sharing platforms, Airbnb has faced widespread opposition. Airbnb is a website – a self-described "community marketplace" – linking people who have lodging to spare with those looking for a place to stay.[32] As one reporter observed: "While Airbnb's popularity has grown, cities across the nation are struggling with how to regulate the impact of those short-term rentals and homestays."[33] Landlords have in many instances opposed the use of leased premises because Airbnb rentals are violations of housing laws.[34] The hotel industry and regulators have argued that Airbnb circumvents taxes that must be assessed on hotel room occupancy.[35] Responding to this issue, Philadelphia enacted a law allowing and taxing short-term home and room rentals.[36]

> On-demand businesses like Uber, Lyft, GrubHub, and Instacart are revolutionizing commercial behavior by using technology, often via phone apps, to immediately link the consumer to a good or service

Airbnb has responded similarly to Uber in stating that it is not a hotel or lodging provider, but is merely a platform to connect a willing supply of lodging to a willing demand of guests needing housing.[37] Airbnb has elected to educate its users that they may have obligations as hosts to inform themselves of their obligations in their jurisdiction and to comply with all permitting, licensing, and tax paying obligations.[38] Where Airbnb hosts have operated in a manner that appears to qualify as illegal hotel operations, Airbnb reports that it has removed such users from its systems.[39]

Airbnb and similar on-demand companies face issues that, inevitably, must be addressed. Practitioners around the country and the globe will likely continue to see these fights at the state and local government levels, in the courts, and in the media.[40] Attorneys must be informed and prepared to apply old concepts, such as worker classification, to novel situations. Likewise, lawmakers and regulatory agencies must be prepared to create new legislation and regulations to respond to emerging issues.

Crowdfunding

Crowdfunding is "the practice of funding a project or venture by raising many small amounts of money from a large number of people, typically via the Internet."[41] Unlike traditional investing, crowdfunding campaigns are funded by the general public; successful projects typically receive about 25-40% of their funding from their first, second, and third degrees of connections.[42] This is accomplished through crowdfunding platforms – such as Kickstarter, Indiegogo, RocketHub, and Onevest – which allow consumers to ask for or donate money.[43] Crowdfunding platforms are used to raise money for everything from launching a new tech venture to raising money for a local charity.[44] Kickstarter is a common launching pad for art and film projects.[45] It is a hub for inventors as well, and five of *Time's* 25 best inventions for 2014 were Kickstarter projects.[46]

Crowdfunding gained traction in the U.S. three years ago, when Congress approved the Jumpstart Our Business Startups Act ("JOBS Act").[47] The JOBS Act enabled and inspired new funding models and, ultimately, led to crowdfunding opportunities such as private equity investing by unaccredited investors and peer-to-peer lending for all investors.[48] In March 2015, the SEC issued a provision of the JOBS Act allowing for unaccredited investors to invest in private companies.[49] Lawyers must decipher the legal landscape of fundraising and capital access for start-up companies and small businesses. Crowdfunding is rapidly gaining popularity and, as it becomes more prevalent, so too will the necessity for attorneys to understand the associated legal and regulatory issues.[50]

Back in 2012, scholars asserted that crowdfunding was a "legal disaster waiting to happen."[51] In some ways, it appears this prediction has come true. For a lawyer advising clients on fundraising, the pitfalls and potential problems are many. Despite its apparent legality, crowdfunding, depending on how it is conducted, can be fraught with securities violations, intellectual property infringements, privacy violations, and even emerging cyber-legal issues.[52] Not only do crowdfunding platforms carry a host of new legal issues, but they also create new twists on well-established legal issues such as taxation, contracts, and even corporate law.[53]

One question facing the industry is whether (and to what extent) crowdfunding consumers merit protection from potentially deceptive or unfair marketing.[54] Currently, there is very little consumer protection.[55] Many of the funded projects struggle with timely completion of goals, and some never deliver the promised products.[56] Last year, the Washington State Attorney General brought a consumer protection lawsuit against a crowdfunded company that failed to deliver playing cards that it promised to funders.[57] Recently, the Federal Trade Commission took its first-ever action over a crowdfunding project, concluding that its creator used "deceptive tactics" by raising more than $122,000 – purportedly to create a board game – and spending the money on rent, moving, and personal items.[58] However, neither the FTC nor the Washington State litigation involved actions against the crowdfunding platform. The FTC will continue to scrutinize crowdfunding, and future litigation will also likely help to shape how consumer protection should be addressed within the field.

It is too early to predict what effect crowdfunding will have on the established investment industry. With the finalization of the JOBS Act's crowdfunding rules, innovators have yet to make the big splashes that on-demand businesses like Airbnb, Uber, and Lyft have made. As opportunities open up for entrepreneurs to utilize the economic power of crowdfunding, it is anyone's guess as to what industries will be disrupted. As the investment world evolves, so too will our role as counselors and advocates in navigating the new territory.

Conclusion

This analysis of on-demand companies and crowdfunding has left only one undeniable truth: innovations are constantly shaping the legal field. So how does a lawyer in today's cyber-centered marketplace prepare for these fast-evolving and new legal issues? The answer is that we, more than ever, must be students of our practice areas. We must be prepared to learn how emerging technology is shaping and affecting the law, and must learn about the industries and the client's plans to spot issues before they arise. We must be open-minded in considering new applications of old legal maxims and standard legal forms. Importantly, we must seek to anticipate how a client's actions, whether in the context of website marketing or in crowdfunding a project on Kickstarter, will bear out in a legal context.

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Lucas E. Buckley...

is a native of Gillette, Wyoming, and practices at Hathaway & Kunz in the areas of civil litigation—including business and commercial litigation and risk management—as well as catastrophic injury representation for both plaintiffs and defendants. Mr. Buckley delivers high-caliber, personalized representation by working with clients to discover their unique needs and goals before developing a legal strategy.

Mr. Buckley is also experienced in energy and natural resource matters, including due diligence, title and land use, curative work and regulatory compliance. Recognizing the importance of mutual trust between attorney and client, Mr. Buckley maintains the utmost transparency in communication. He enjoys helping clients to find a positive solution to a complex problem that has left them feeling lost.

Jesse K. Fishman...

joined Hathaway & Kunz in December 2014. Her practice focuses on business formation, commercial litigation, property disputes, and personal injury matters. She also advises clients on a broad range of employment and transactional matters, including entrepreneurial and start-up issues. Before joining Hathaway & Kunz, Ms. Fishman worked at an insurance defense firm in Denver handling cases involving personal injury, professional liability, employment law, and municipal defense.

Matthew D. Kaufmann...

is a partner with Hathaway & Kunz. Mr. Kaufman's practice centers on business, corporate, transactional, and litigation matters. He takes pride in counseling his clients with the highest level of responsiveness, diligence and legal expertise.

With an advanced LL.M. degree in entrepreneurial law, Mr. Kaufman is well-equipped to provide highly-skilled representation to entrepreneurs, start-ups and emerging companies—as well as established businesses and companies—on complex transactions and strategies. He routinely represents and advises clients on matters such as: entity formations, financing and operational issues, intellectual property protection, mergers and acquisitions, regulatory compliance, and contractual disputes. Mr. Kaufman is extensively involved in local and regional entrepreneurship, and particularly enjoys facilitating a start-up business's development into a successful company.