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Texas may consider how transportation network companies are regulated

In May 2016, Uber and Lyft suspended operations in Austin in response to certain regulations passed by the Austin City Council. The withdrawal of the two most prominent transportation network companies (TNCs) from the Texas capital drew nationwide attention to state and local laws on these services.

TNCs compete directly with taxicabs to fill the gap between public transit and private vehicle ownership, providing on-demand transportation without the cost of owning a vehicle. Other primary users of taxicabs and TNCs include tourists and visitors, the elderly or people with disabilities who need private transportation to vital services, such as doctor's appointments, and those who need sober rides home.

In Texas, TNCs are subject to regulation mostly by municipalities, with state regulation thus far focused on insurance requirements. Some say TNCs should be regulated locally to ensure public safety, accessibility, and accountability to passengers and the public. Others say state government is better suited to regulate TNCs because it would create uniform standards and reduce compliance costs. This report examines the TNC business model, current state and local laws governing TNCs, and policy proposals the 85th Legislature may consider during its regular session.

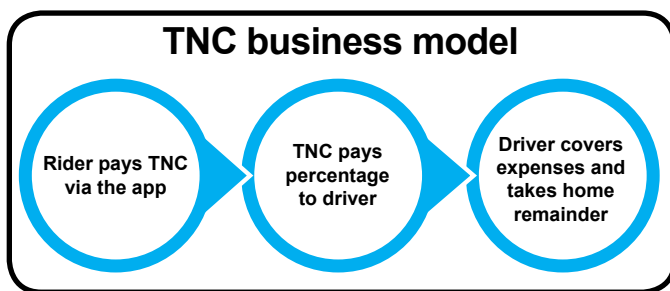
This report explores how TNCs are regulated by state and local laws in Texas and reviews some proposed legislative approaches.

The business model

TNCs, such as Uber and Lyft, are businesses that provide platforms to connect paying riders to drivers. TNCs differ from traditional taxicab and limousine services in that the TNC driver uses a personal vehicle, rather than a commercial one, and is not required to work a specific schedule. TNC platforms usually take the form of smartphone apps or websites through which passengers can request rides,

sending their precise locations to nearby drivers via GPS. Some TNC services allow customers to schedule rides in advance.

TNCs make money by taking a cut of the total passenger fare, usually about 20-30 percent, and passing the remainder, minus any local fees, on to drivers, who operate as independent contractors. Litigation is ongoing in some states over whether drivers should be classified as employees rather than independent contractors, which would require TNCs to be responsible for certain operating costs and unemployment insurance.



Current Texas law

TNCs were not subject to specific state regulation in Texas until 2015, after the regular session of the 84th Legislature. Before this, the section of state law most relevant to the industry was Local Government Code, [sec. 215.004](#). Some cities applied the regulations developed under this authority to TNCs, while others wrote new regulations or changed their ordinances. In effect since the enactment of SB 564 by Whitmire in 1987, [sec. 215.004](#) requires certain municipalities to license, control, and regulate taxicabs. It also allows cities to regulate market entry and rates and to establish other requirements to ensure safe and reliable transportation. In 2007, [HB 2338](#) by Bailey expressly allowed cities to regulate limousine services.

The 84th Legislature in 2015 enacted one bill on TNCs, among several that were considered. [HB 1733](#) by Smithee, which took effect January 2016, requires TNC drivers or companies to maintain primary auto insurance that is active any time the driver is logged onto the TNC's network. Liability limits for this policy must be at least \$100,000 for bodily injury to or death of a person, per incident, and \$25,000 for damage or destruction of

property. However, for the period of time between a driver accepting a ride and all passengers exiting the vehicle, the policy must have a minimum upper limit of liability of at least \$1 million for each incident. If a driver's insurance policy has lapsed or is insufficient, the TNC must provide coverage, beginning with the first dollar of a claim against the driver.

Previous proposals in Texas

Bills filed but not enacted in 2015 included [HB 3358](#) by Lucio, which died in the Calendars Committee. It would have amended Local Government Code, [sec. 215.004](#) to require certain municipalities to license, control, and regulate all passenger transportation services for compensation, including those provided by TNCs. [SB 1555](#) by Eltife, which did not receive a hearing, would have required transportation network companies to be licensed by the Texas Department of Licensing and Regulation.

The most comprehensive bill on TNCs that the 84th Legislature considered was [HB 2440](#) by Paddie, which died in the Calendars Committee. It would have established a statewide regulatory framework for TNCs while prohibiting certain local requirements. Under the bill, municipalities could have required TNCs to access the Department of Public Safety's electronic clearinghouse for background checks on drivers and could have enacted ordinances on TNC services at airports. The bill would have required TNCs to pay a \$115,000 annual fee for a permit issued by the Department of Motor Vehicles (DMV) before operating in the state.

HB 2440 would have established driver standards, including how to handle complaints about drug or alcohol use by a driver while the driver was logged onto the TNC's platform. Under the bill, drivers would have been required to submit to a background check that searched the national sex offender registry and that covered multiple states and jurisdictions with primary source validation. Municipalities could have required TNCs to access the fingerprint database maintained by the Texas Department of Public Safety. Drivers would have been disqualified for a certain number of previous convictions for moving violations, driving while intoxicated, or certain other crimes.

The bill would have included provisions on accessibility, allowing the DMV to impose a fee of up to

\$10,000 on any vehicle-for-hire company, including TNCs and taxicab and limousine companies, that did not provide wheelchair accessible service and would have prohibited charging more for such services. The money generated would have been used for grants to companies providing wheelchair accessible service.

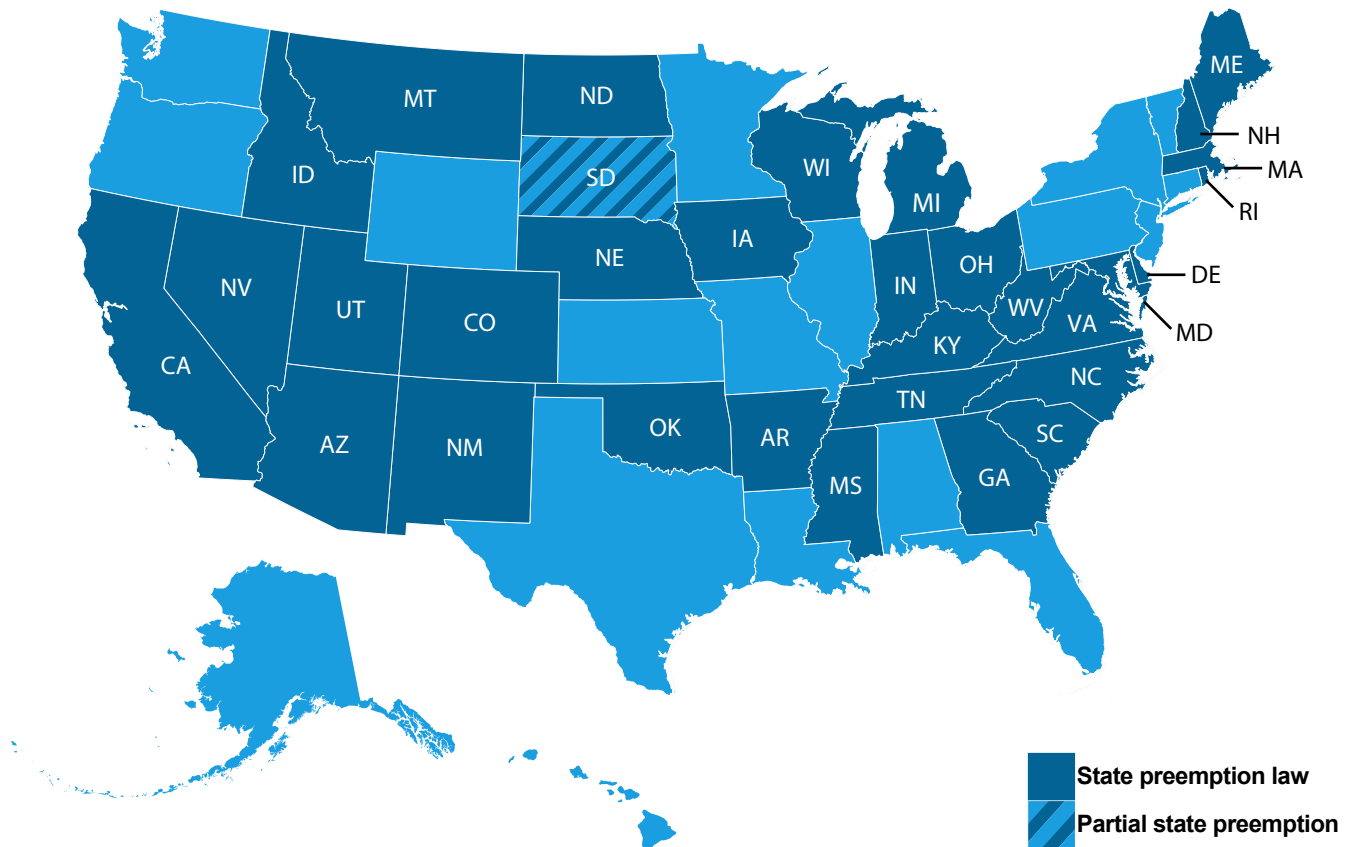
The DMV would have been authorized to suspend or revoke a TNC permit for violations. The bill would have allowed the DMV Board to request that the attorney general pursue a civil penalty of up to \$10,000 per violation.

Local regulations in Texas

TNCs in Texas are regulated primarily by municipalities, aside from the statewide insurance regulations enacted by the 84th Legislature. TNCs are not active in all cities that have adopted regulations. Local regulations address accessibility, permitting, driver requirements, and pricing, among other issues. The charts on pages 4-5 outline some local TNC regulations in Texas.

Fingerprint background check. Some cities require that potential drivers undergo a fingerprint background check before receiving a driver’s permit or otherwise being allowed to operate a vehicle for hire. Cities may allow

States that preempt local TNC regulations



According to [TTI](#), as of November 2016, 42 states and the District of Columbia have passed legislation relating to TNCs. Of those states, 31 preempt local authority to regulate TNCs. In addition, South Dakota preempts local requirements relating to minimum insurance coverage for TNC drivers but not for other regulation.

Source for information: Texas A&M Transportation Institute (TTI), HRO research

drivers to operate under a provisional permit for a short time before receiving the results of the background check. See *Debate on fingerprint background checks*, page 6.

Company operating permit. Some cities require TNCs to receive operating permits before doing business in the city’s jurisdiction. These permits typically require the TNC to demonstrate or assert that all drivers meet a set of criteria and that the TNC has insurance that meets or exceeds certain standards. They may require TNCs to report certain data to the city upon request. Failure to meet these requirements can result in the revocation of the TNC’s operating permit.

City driver permits. Some cities require individual drivers to get approval from the city before driving for a TNC. This is typically in the form of “vehicle-for-hire permits” or “chauffeur’s licenses.” Cities that do not require such permits or licenses often instead require the TNC to certify that all drivers meet certain standards, and they reserve the right to revoke the TNC’s operating permit.

Amarillo and Galveston both require potential drivers to undergo a physical exam by a licensed physician before receiving a city driver permit. These exams check the driver’s eyesight and look for evidence of infectious disease, emotional instability, drug addiction, and mental disability.

Dynamic pricing. Some TNC platforms automatically increase prices during periods of high demand. Some local ordinances prohibit this practice during “market abnormalities,” such as natural disasters or other market disruptions that result in the declaration of a state of emergency by the governor.

Vehicle standards. Some cities have requirements for TNC vehicles beyond state inspections. For example, a vehicle may be required to meet a certain standard of interior and exterior appearance and cleanliness, be manufactured within a certain number of years, have fewer than a certain number of miles, or have four doors. Cities also may mandate that vehicles pass inspections broader than the state inspection or be approved by a city official.

Regulation in Texas cities, pop. 200,000 or greater

	Austin	Corpus Christi	Dallas	El Paso	Fort Worth	Houston	Lubbock	San Antonio*
Fingerprint background check? **	Yes	Yes	No	No	No	Yes	No	Optional
Company operating permit required?	Yes, fees vary	Up to 2% of gross	\$282+\$3 per vehicle	\$300	\$500	2% of gross	\$250	\$10,000-\$50,000 per year
City driver permit required?	Yes	Yes	Yes	No	No	Yes	No	No
Dynamic pricing limited?	Yes	No	No	Yes	No	No	No	No
Vehicle standards (other than state inspection)?	Yes	Yes	Yes	No	No	Yes	No	Yes
Hours active on network limited?	12 per 24 hours	12 per 24 hours	No	No	No	12 per 24 hours	No	No

Ordinances identified by [Texas Transportation Institute](#) and various TNCs

*Information reflects operating agreements between the city and individual TNCs that override city ordinance

** See *Debate on fingerprint background checks*, p. 6

Source for information: U.S. Census Bureau, city ordinances as of January 2017

Accessible vehicle requirements. Most local ordinances require that TNCs not discriminate based on disability and not charge a fee for wheelchair-accessible service or for people with service animals. Most require the TNC to adopt a nondiscrimination policy and either provide accessible service or direct passengers to an alternative provider. Houston requires TNCs to either have a certain number of wheelchair accessible vehicles or successfully provide, on average, accessible service within a certain time. Austin requires TNCs to submit accessibility plans within six months and provide in-app accessible services or alternatives within three months of obtaining operating authority.

Street hails. Most Texas cities with TNC regulations prohibit drivers from accepting riders who flag them down as they would a taxicab. Cities note that allowing street hails can lead to gaps in insurance coverage, where neither the driver’s personal insurance nor the TNC’s insurance covers the passengers because the ride was not negotiated through the TNC platform. TNCs also usually have internal policies prohibiting drivers from accepting street hails.

Display of company logo/emblem. Austin, Corpus Christi, Houston, and Lubbock require a vehicle to display trade dress, such as a logo or emblem, signifying that the vehicle is being used to provide transportation services.

Recent proposals in Texas

Committees in the Texas House and Texas Senate held interim hearings on TNCs in 2016. Four bills that address TNCs — [HB 100](#) by Paddie, [SB 113](#) by Huffines, [SB 176](#) by Schwertner, and [SB 361](#) by Nichols — have been filed thus far for the regular session of the 85th Legislature.

All filed bills about TNCs as of February 2017 would preempt most or all local regulation of TNCs. Some of the proposed legislation also would preempt local regulations on taxicabs and limousines, while some would expressly allow airports to regulate TNCs providing rides to or from the airport. The 85th Legislature may consider these and other proposals during the 2017 legislative session.

Regulation in Texas cities, pop. less than 200,000

	Abilene	Amarillo	Beaumont	College Station	Galveston	Longview/Tyler	Midland/Odessa	New Braunfels	San Marcos
Fingerprint background check? **	No	Yes	No	No	Yes	No	No	No	No
Company operating permit required?	\$500	\$100+\$75 per vehicle	\$100	\$300-\$1,200	\$120 per vehicle	\$250	\$1,500	\$500	\$400
City driver permit required?	No	Yes	No	No	Yes	No	No	No	No
Dynamic pricing limited?	Yes	No	No	Yes	No	No	No	No	Yes
Vehicle standards (other than state inspection)?	No	Yes	No	No	Yes	No	No	Yes	No
Hours active on network limited?	No	No	No	No	No	No	No	No	No

Ordinances identified by [Texas Transportation Institute](#) and various TNCs

** See Debate on fingerprintbackground checks, p. 6

Source for information: U.S. Census Bureau, city ordinances as of January 2017

State preemption of local rules

One proposal adopted in at least 31 other states is to prohibit certain municipal regulations on TNCs and establish state regulations in their place. Some say state preemption is necessary to make rules more consistent across local jurisdictions and to decrease barriers to entry for drivers, while others say local governments are better suited to enact rules that meet local needs.

Supporters of state preemption of local rules on TNCs say eliminating the patchwork of local rules would help increase the number of drivers and enable Texans to find convenient transportation. Local rules create barriers to entry in each market, they say, and can cause demand for transportation to overwhelm supply, resulting in long wait

times and acting as a bottleneck on the economic benefits of TNCs.

With statewide preemption, drivers could serve multiple cities without applying for a new driver permit in each city. TNCs and drivers currently need city-specific permits in many municipalities. However, it is not unusual for TNC drivers to travel from one city to another for major events or across metroplexes during a day, supporters say, and the regulatory framework should reflect that reality.

State preemption also would allow burdensome local regulations to be eliminated, supporters say, which would give citizens easier access to a source of income when needed. TNCs say the average driver seeks to work part time to supplement or temporarily replace income. They

Debate on fingerprint background checks

TNC drivers must undergo fingerprint-based background checks in some cities in both Texas and other states that have not preempted local regulation. No state government requires fingerprint background checks. Critics of these checks say they would impose costs on TNCs without improving safety, while supporters say passengers would be at greater risk without them.

Supporters of requiring fingerprint background checks say it would reduce risk to passengers and therefore be worth the added cost. Fingerprint background checks are considered the gold standard because they involve more records and reveal more information than other methods. Other forms of background checks may be vulnerable to fraud and misidentification, supporters say, but fingerprints reduce the chance of failing to identify someone with a criminal record. Commercial background checks search for court records only in specific jurisdictions and can miss those not searched. The City of Houston has [reported](#) that several applicants for vehicle-for-hire licenses who passed a commercial, multi-state background check were later found by a fingerprint background check to have committed serious crimes. Despite concerns of opponents, supporters say, fingerprint checks are not discriminatory. Current rules do not necessarily disqualify applicants based only on an arrest record, and applicants may appeal and present more information. TNCs operate in many cities under local regulations of some kind, showing the state can realize the benefits of TNCs while adequately regulating them.

Opponents of requiring fingerprint background checks say they add costs without improving passenger safety. TNCs already use accredited multi-state commercial background checks and screen against the national sex offender registry. Opponents say security features built into TNCs, including GPS tracking, driver photos, and standards based on rider reviews, provide acceptable rider safety. According to opponents, fingerprint checks could unfairly bar some drivers because the fingerprint records sometimes reflect arrests but not convictions. Some reports note that about half of arrest records in the FBI's background check system may lack information about final case outcomes. A report from the Bureau of Justice Statistics indicates that about a third of felony arrests in the most populous U.S. counties did not result in convictions in state courts. As a result, using fingerprint databases to screen drivers could lead to discrimination because in many cities the arrest rates are higher for African American and Hispanic populations than for white populations. Opponents say TNCs should be allowed to use internal policies to hire drivers, as customers will use services that protect riders and avoid those that do not. No transportation option is entirely safe, they say, so consumers should not be forced to accept the higher costs associated with fingerprint background checks.

may not make enough to offset large upfront costs, such as for fingerprinting and driver physicals, which drivers often are expected to pay for themselves. State preemption of such rules would allow citizens to quickly supplement income after a job loss or other economic setback.

Preempting burdensome local rules also could increase access to transportation, which benefits consumers, businesses, and public safety. TNCs in local markets enable people to save time and spend more money on what they value. They also provide a vital service to local businesses, which depend on reliable sources of transportation for consumers. More transportation options also can lead fewer people to drink and drive. However, costs of local regulations may reduce availability of services by reducing incentives to drive. A Temple University study found the least expensive level of Uber service alone led to a reduction of up to 5 percent in motor vehicle homicides, largely caused by drunk driving, per quarter in California.

While some opponents have said state preemption would infringe improperly on local control, supporters say state preemption is acceptable when local control does not protect liberty because local control is a tool, rather than an end goal. Unlike the state's relationship to the federal government, Texas municipalities are creations of the state, which grants their powers, so it is acceptable for the state to limit local control of TNC rules, supporters say.

Opponents of state preemption of local rules on TNCs say local regulations ensure that TNCs, which can be large, multinational corporations worth billions of dollars, are held strictly accountable to local standards. Municipalities that craft their own rules can adapt them to local circumstances, opponents say. City officials are closer to constituents and better able to create policies reflecting the local will. Austin voters showed support for local rules by defeating a referendum that would have nullified the city's regulations. Opponents of state preemption say localities should be allowed to maintain a level of public safety that suits their citizens.

Local rules do not deny potential drivers a chance to earn money because they do not substantially slow the process of signing up to drive, opponents say. Most municipalities that require city-approved TNC licenses issue provisional ones that allow a driver to drive temporarily while completing the application process. Provisional licenses allow a driver to begin work quickly while maximizing public safety and realizing societal benefits, such as reduced drunk driving.

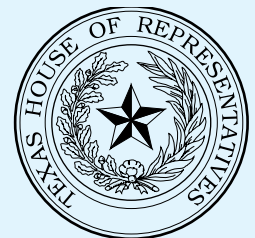
Municipal regulations are not an excessive burden, according to opponents. TNCs operate and expand in cities with stringent requirements, and these cities have not seen a shortage of drivers.

Opponents say lawmakers should not exacerbate the effects of an unfair playing field by preempting regulations on TNCs but not on taxicabs, which provide the same basic public service. Taxicabs generally are heavily regulated at the local level and subject to limits on fares, vehicle appearance, and number of vehicles, putting them at a disadvantage to TNCs without such restrictions.

Opponents of state preemption say local control itself is a valuable objective, as preemption would increase the distance between regulators and those affected by TNCs. They say local regulators are more responsive to individual concerns and thus more effective at holding TNCs accountable and ensuring public safety.

— *by Anthony Severin*

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