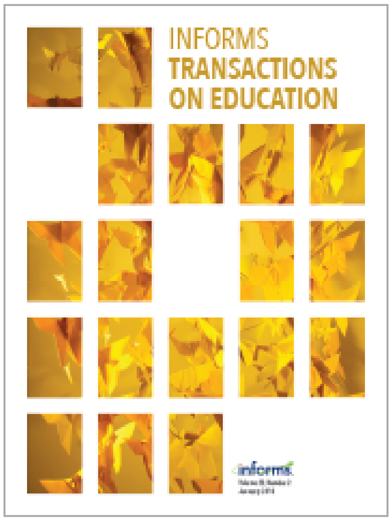

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Case

The Rise and Fall of Taxi Club Management in New York

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Taxi Club Management, or TCM for short, was a major taxi operator based in New York City (NYC). Up until 2013, NYC taxi medallion (the taxi license attached to the hood of a taxi) prices were on a meteoric ascent, with each medallion being valued at upwards of $1 million. However, the company's fortunes soon went south when Uber, the popular ride-sharing application, rolled into town and started competing directly against the NYC Yellow Taxi Industry (which included TCM and other "medallion" or yellow taxi operators), lowering medallion prices on a massive scale and leading to a drastic drop in TCM's valuation. The situation became so severe that in September 2016, the company was evicted from its headquarters located in the neighbourhood of Chelsea, Manhattan, when TCM's owner, taxi tycoon Gene Freidman, was unable to pay more than $77,000 in back rent owed to the landlord of the property space (Ross and Rivoli 2016).

What were the factors that led to TCM's current situation, and what could the company's owner, Gene Freidman, have done differently to salvage his company from financial ruin?

History of New York City Medallion Taxicabs

Since 1907, the year when the first metered taxis were introduced to the streets of New York City, taxicabs were woven into the city's cultural and social fabric. Driven mainly by African American or Middle Eastern immigrants, for many Americans, taxis were symbols of hope, promise, and dreams of a better life (National Public Radio 2007). This idea was so ingrained into the city's heritage and beliefs that it sparked the creation of the ground-breaking television series *Taxi*, which chronicled the lives of employees of the fictional NYC-based Sunshine Cab Company and described their struggles to move up in social class and achieve financial success.

A large part of the reason why so many people associated the NYC taxi industry with opportunities for social mobility was the value of the medallions—tiny tin seals attached to the taxi's hood that authorize drivers to operate (National Public Radio 2007). These medallions essentially functioned as taxi licenses; only taxis with medallions attached could conduct business in the Manhattan borough, the busiest and most densely populated area of New York City. Due to the limited space and narrow roads of Manhattan, the New York City Taxi and Limousine Commission (TLC), the government agency responsible for issuing these medallions, had historically offered an extremely low number of these prized and highly sought-after seals. A medallion can be described as "an asset that may be sold or pledged as collateral loan" and as "the exclusive right to accept street hails" (Durden 2013). TLC offered two types of medallions—an individual medallion aimed at a sole proprietor and a minifleet medallion aimed at corporations that manage a fleet of taxis through the ownership of multiple medallions.

In 1937, the TLC limited the number of circulated medallions to 11,787 due to the passage of the Haas ordinance. The Haas Act "mandated that 60 percent of [taxi] medallions go to fleets that could rent them to drivers," essentially allowing companies flush with cash to obtain these medallions and then wait for them to increase in value (van Gelder 1996). As a result of the Haas Act, the number of medallions stayed constant at 11,787 from 1937 to 1996. In 2015, close to a decade after the number of medallions could increase again, total medallion count was just 13,587, representing only a 15% increase in issued medallions over nine years (New York City Taxi and Limousine Commission 2016).

The scarcity associated with taxicab medallions had caused their value to skyrocket, from $2,500 per medallion in 1947, to $1.32 million per medallion in 2013 (Van Zuylen-Wood 2015). A large part of this inflation in value was due to the TLC's unique method of issuing medallions—through public bidding auctions. Interested parties had to submit bid packages, which included among other things, the bid amount, a completed and approved TLC medallion license application form, and a letter of intent that covered 80% of the submitted bid price.

Background of Taxi Club Management

Because of the sharp increase in medallion value, taxi operators saw huge opportunities in obtaining medallions to use as long-term investments on the assumption that prices were likely to go up because of their limited availability. Taxi Club Management was one of many companies to take advantage of rising medallion prices, but was arguably one of the most successful, as the company operated approximately 860 taxis in New York City, more than any other company in the area (Van Zuylen-Wood 2015).

The founder of Taxi Club Management, Evgeny (a.k.a. Gene) Freidman, was himself an immigrant, having been born in the Soviet Union in 1970 and then emigrating to the United States as a political refugee in 1976 (Freidman 2015). When Friedman and his family settled in New York City, his father decided to become a taxi driver in the mid-1970s and went on to manage a taxi fleet of more than 50 taxis. As for Freidman, he studied at the Bronx High School of Science, was a student at Skidmore College, and then obtained a law degree from the Benjamin N. Cardozo School of Law. Shortly after he graduated from law school, he became a financier in Russia, and the business acumen that he acquired from that career proved useful when, in 1996, he obtained control of his father's entire taxi fleet. From then on, noticing the meteoric rise in medallion prices due to the limitation set by the government regarding its supply, Freidman continued to buy taxi medallions, until Taxi Club Management owned the most taxi vehicles in New York City.

Over the years, Taxi Club Management had faced its share of new entrants that threatened the survivability of its business. For example, in December 2011, New York City Mayor Michael Bloomberg announced that New York Governor Andrew Cuomo was signing a new piece of legislation called the "State Livery Law." Included in the law was a bill called the "Five Borough Taxi Plan" that introduced a new classification of taxis—the Boro taxis. In comparison with the traditional medallion taxis, these taxis were painted a light green color named "Big Apple green" instead of yellow, and they were allowed to pick up passengers only in selected regions of the city, including the outer boroughs (such as the Bronx, Brooklyn, and Staten Island) and the northern part of Manhattan. Previously, only licensed medallion cabs could respond to street hails or booking calls in these areas. As a direct consequence of this bill, there would have been increased competition for taxi passengers in the outer boroughs and selected areas of Manhattan. Although the enactment of the taxi plan undoubtedly affected the profitability of medallion taxi drivers and taxi fleet companies, so much so that the entire yellow cab industry banded together to sue the state government in mid-2012, the impact of this legislation paled in comparison with the protests that would happen as a result of Uber offering its services in New York City.

Uber

Uber Technologies Inc. was a ride-hailing software service provider headquartered in San Francisco, California. It was one of many companies to belong to a burgeoning category of products and services called the "multi-sided platform" (MSP). MSP referred to any interface/platform that essentially facilitated interactions between two or more participant groups that were also users of the MSP (Van Alstyne et al. 2016). In Uber's case, the two groups in question were the drivers, who either owned their own private vehicles or were renting them from third parties such as rental companies, and the consumers who were looking for a ride to their intended destination.

The main reason why Uber's massive expansion into 81 countries and more than 580 cities worldwide had stirred up so much controversy was because of the company's disruptive business model. Unlike taxi companies that generally owned their own taxi fleets, Uber generally relied on car owners to supply their own vehicles, although in some markets, Uber set up a car rental company. If a person wanted to become an Uber driver but had no vehicle of his or her own, the potential driver was expected to source for a vehicle independently. Furthermore, Uber drivers needed only to be at least 21 years old with a driver's license. Uber also attracted traditional taxi drivers to join them through sign-up bonuses, lower rental rates with Uber partners, and other incentives.

Uber drivers were not considered as employees, but rather as independent contractors. This meant that Uber drivers were not entitled to certain employee-only benefits such as Social Security and minimum wage (Isaac and Scheiber 2016). These decisions allowed Uber to experience huge cost reductions compared with traditional taxi firms, as Uber would not incur costs associated with keeping a taxi fleet, such as maintenance and repair costs. In return, Uber could then make its services more attractive to consumers through lower ride prices and more frequent promotions. In contrast, fares in the traditional taxi industry were regulated by TLC. Consequently, TCM must obtain approval from TLC if TCM intended to deviate from standard fares. In contrast, Uber's fares were unregulated.

A key aspect of Uber was its app that enabled matching of customers with drivers. The app made use of Global Positioning System (GPS) so that customers could view the location of drivers and vice versa. The app also allowed the drivers and customers to rate each other. However, unlike other MSPs such as eBay, or even third-party sellers on Amazon, the positive network effect from ratings was less pronounced, as customers did not get to choose their Uber driver. But this option might be available in future. At best, customers could cancel the assigned driver, which came at the cost of added waiting times.

Uber's Entrance into New York City

Even though Uber began its New York City operations in 2011, its presence was not truly felt until 2014. By then, Uber had expanded its New York City fleet from 7,000 to 16,000 and began offering a host of services. These services were meant to tempt consumers to switch from hailing taxis to hailing Uber vehicles.

As of January 2017, Uber offered a wide variety of rides in New York City, including the following:

- UberX was the most basic ride service offered by Uber. Although the calculated fare paid for an UberX ride was similar to the metered fares used by traditional taxi industries in that it included a base fare, per-minute fare, and per-mile fare, Uber also offered a fare estimator that was an in-built function of the official Uber app that automatically calculated the approximate cost of a ride, after passengers had input their starting point and ending destination. This unique approach to fare calculation reduced passengers' uncertainty regarding the amount of money they would be charged by providing them with more payment information at the outset, even before they had booked their rides.
- UberXL was similar to the UberX but was meant for carrying larger groups of passengers. Whereas UberX vehicles typically accommodate only up to four passengers, UberXL vehicles (that comprise SUVs/mini-vans instead of cars) could fit up to six.
- UberBLACK was the high-end, luxury version of the UberX service; Uber described it as "a high-end chauffeur experience for a fraction of the cost" (Uber Technologies Inc.). The main difference in these services lay in the car models used for each service; whereas UberX vehicles were mainly manufactured by mass-market automobile brands such as Toyota, Nissan, and Hyundai, UberBLACK vehicles came from luxury car brands such as Porsche, Mercedes, Bentley, and Rolls-Royce. Understandably, as UberBLACK was being advertised as a premium service, a single ride would cost considerably more compared with the UberX option.
- Similar to the relationship between UberX and UberBLACK, UberSUV was a premium, more exclusive version of the UberXL. The Uber website described this service using a simple equation: "UberXL + UberBlack = UberSUV" (Uber Technologies Inc.).
- UberPOOL was Uber's carpooling offering and was arguably the most affordable service out of its entire lineup. The service was mostly aimed at price-sensitive consumers who did not mind carpooling with a complete stranger who was heading in the same direction in exchange for paying a lower fare. This service was one of the main ways in which Uber differentiated itself from traditional taxi firms, as those companies did not offer such a service.

Another important aspect of Uber's business model was the company's use of surge pricing, which was the primary way in which Uber implemented dynamic pricing. Surge pricing ensured that Uber's fares reflected the current demand for its services, by using an automated algorithm to detect when certain areas of the city were experiencing high demand. For instance, during 5–7 p.m. on weekdays, demand for taxi services in downtown Manhattan usually increased because most working adults had just finished work and were looking for a quick and easy way to get back home. During this peak period, Uber's surge pricing would activate, and all of the fares for rides beginning in the downtown Manhattan area would be increased by a specific multiplier, which was displayed in the app (e.g., 1.5× or 2.0×). This multiplier was calculated by Uber's algorithm, and then instantaneously shown in the app interface. However, once demand had dropped below a certain level determined by the algorithm, surge pricing would cease and the multiplier would be removed. This constant monitoring of demand allowed Uber to practise revenue management effectively. It also ensured that the demand for its rides would never outstrip supply by a huge amount. The reason is that the more price sensitive a consumer is, the less likely he or she would still want to take an Uber ride after surge pricing kicked in. This would reduce the overall demand during the high-volume periods.

Uber's Impact on Taxi Club Management

When Uber first entered New York City, Freidman was not worried about the heightened competition. He himself had thought about developing an application for his taxi fleet business, and, when asked about his thoughts on Uber, said "Uber's not a problem" (Van Zuylen-Wood 2015). However, his tone soon shifted when he noticed the rapidly decreasing value of taxi medallions. A single medallion, once valued at $1.3 million in 2004, has drastically dropped to just $250,000 by 2016, a stunning 80.77% decrease in valuation. The share of passengers that chose to ride taxis dropped from 84% in April 2015 to only 65% one year later (Holodny 2016). To make matters worse, in July 2014, Lyft, another popular MSP, began offering its services in New York City as well. Although Lyft's late entry meant that it never gained as much traction as Uber because of Uber's well-established network effects, Lyft was still one more competitor that Taxi Club Management had to contend with.

Furthermore, the entrance of Uber and Lyft had impacted not only the demand for taxi services but the supply of taxi drivers as well. Even though medallion prices had dropped sharply, they still represented a significant investment for ordinary people looking to become taxi drivers. Furthermore, fleet owners such as Taxi Club Management were charging substantial rental fees. As a result, more people were choosing to work under Uber as independent contractors rather than pay the relatively high fees associated with being a taxi driver. Not surprisingly, as of January 2017, there were approximately four times more private ride-sharing vehicles along the streets of New York City than taxis. Specifically, there were 46,000 ride-sharing vehicles associated with Uber, whereas the number of taxis had stayed relatively stagnant at 13,587 (Hu 2017).

Embracing Change

Freidman had drastically shifted his perspective on Uber. What was once a company that he claimed would not be a problem to his business was now the "nastiest, most morally corrupt company ever," according to an interview Freidman gave to *Bloomberg* (Van Zuylen-Wood 2015). Furthermore, there were signs that Freidman was tweaking his business strategy to contend with the threat that Uber was posing to Taxi Club Management. In 2016, news emerged that Freidman was working closely with a company called Flywheel to introduce an electronic-hailing application that would be used in conjunction with New York City taxis. The app not only would allow passengers to call for a cab remotely but also came with a backend operating system named "TaxiOS" that allowed taxi drivers to use a smartphone to perform critical functions, such as meter monitoring, accepting dispatch notifications, and processing credit card payments. Flywheel hoped to roll out this service to every single medallion taxi by the end of 2017. Even though Freidman was one of Flywheel's key partners, a spokesperson for Flywheel said that the service was not limited to any one fleet, meaning that should this service roll out, Taxi Club Management would not be able to utilize the app's services exclusively. Oneal Bhambani, chief financial officer of Flywheel, even went so far as to describe the app as "giving [taxi drivers]... a weapon to fight back against Uber" (Hawkins 2016). This move was an indication that Taxi Club Management was intending to tackle the "Uber problem" head-on, by utilizing technology that, prior to now, was being used mostly by Uber and other ride-sharing companies rather than by traditional taxi firms.

To what extent could Taxi Club Management's financial woes be attributed to Uber's entrance into New York City? Was there a way for Taxi Club Management to effectively compete with Uber? Would the introduction of Flywheel give Taxi Club Management a competitive advantage?

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