

# **TAXI FARES FOR 2000-2001**

**DRAFT PRICE DIRECTION**

**MAY 2000**



**INDEPENDENT COMPETITION AND REGULATORY  
COMMISSION**

## FOREWORD

The Independent Competition and Regulatory Commission has been issued with terms of reference requiring an investigation into:

- the maximum taxi fares for taxi services provided within the ACT for a period of between three to five years; and
- the recommended method or formula as appropriate which may be used.

The Commission has prepared a Draft Prices Direction and now makes this draft available for public comment. The Commission has not sought to set a price path for a three to five year period at this time. Rather the Commission has preferred to set a price level for the 12 month period from 1 July 2000. As part of that price structure, the Commission has recommended what should be the net impact of the introduction of the GST from 1 July 2000.

Comments are now invited on the Draft Prices Direction prior to a Final Prices Direction being issued in early June.

Paul Baxter  
Senior Commissioner  
5 May 2000

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## 1. INTRODUCTION

The Independent Competition and Regulatory Commission (ICRC) has undertaken a preliminary inquiry into taxi fares to apply in the ACT for the 12 month period from 1 July 2000 until 31 June 2001. The terms of reference for this inquiry are included in Attachment 1.

The terms of references establish the tasks to be undertaken by the Commission for this current investigation and the various matters that the Commission is to consider in making this draft pricing direction. Under the terms of reference issued by the Minister for Urban Services, the Commission is required to consider:

- maximum taxi fares for taxi services provided within the ACT for a period of between three to five years; and
- a recommended method or formula as appropriate which may be used to set these prices.

The Commission has considered each of these issues and has made a number of observations and comments upon how prices should be set and what should be the new fares to take effect from 1 July 2000. The Commission has also had to consider the net impact of the GST on fares and to determine an appropriate price adjustment after allowing for any cost savings that might come from the removal of Wholesale Sales Tax and other indirect taxes as part of the proposed tax reform program.

This is a draft report on which comment is sought from all interested parties. This also represents the first formal report by the Commission on taxi fares in the ACT. As such, the draft report seeks to raise a number of issues which pertain to the way in which prices should be set for the taxi industry. The Commission is seeking public comment on these issues prior to any final decision and price direction for the 2000/01 year.

## 2. INVESTIGATION PROCESS

The release of this draft report represents the first stage in a process which is established under the provisions of the *Independent Pricing and Regulatory Commission Act 1997*. The draft report is made available for public comment. The timing for the finalisation of this inquiry is outlined below:

	<b>Date</b>
Draft Direction	5 May
Deadline for comments on Draft Direction	2 June
Final Direction	9 June

Submissions on this draft report should be forwarded to:

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### 3. SUMMARY OF DRAFT PRICE DIRECTION

The draft price direction will set taxi fares to apply in the ACT for a period of 12 months from 1 July 2000, and will incorporate:

- a) a 7.71 percent increase in average taxi charges based on cost increases over the last 12 months;
- b) a net 7.85 percent GST adjustment after allowing for cost savings from the ANTS package;
- c) flag fall, radio fees and waiting time charges to be adjusted to reflect these cost changes with the new rates to be:

Flag fall	\$3.20
Waiting time	\$27 per hour
Radio fee	\$0.65

- d) changes in the various kilometre rates, such that the new rates will be:

Rate 1	\$1.193 per kilometre
Rate 2	\$1.372 per kilometre
Rate 3	\$0.895 per kilometre
Rate 4	\$1.029 per kilometre
Rate 5	\$1.790 per kilometre
Rate 6	\$2.058 per kilometre

- e) the above rates include the net GST adjustment after allowing for cost savings from ANTS.

## 4. STATUTORY REQUIREMENTS AND REGULATED SERVICES

Under the IPARC Act 1997, the Commission is required to have regard to a number of issues in making a price direction. These include:

- the protection of consumers from the abuse of monopoly power...
- standards of quality, reliability and safety...
- the need for greater efficiency...
- an appropriate rate of return...
- the cost of providing the regulated services...
- the principles of ecological sustainable development...
- the social impacts of the decision...
- considerations of demand management and least cost planning...
- the borrowing, capital and cashflow requirements...
- the effect on general price inflation over the medium term; and
- any arrangements that a person providing regulated services has entered into for the exercise of its functions by some other person<sup>1</sup>.

The terms of reference issued by the Minister for Urban Services has identified ‘taxi fares in the ACT’ as the specified regulated service. Previously taxi fares have been set by the Minister with the taxi industry making submissions to the Minister for fare changes. A form of ‘cost index’ has been used to assess variations in taxi operating costs over time. This index has been used for more than 10 years, and fares have been adjusted on a regular basis using this index. In this draft report, the Commission has raised a number of questions about the continued use of the index in its present form.

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<sup>1</sup> Australian Capital Territory, *Independent Pricing and Regulatory Commission Act, 1997, S20(2)*.

## 5. ISSUES CONSIDERED BY THE COMMISSION

Under Part IV of the IPARC Act, the Commission in completing a Determination is required to consider a number of factors and indicate what regard it has had to each factor. The Commission's assessment of each of the Part IV factors is detailed below.

### 5.1 Costs and Efficiencies

Under Part IV of the IPARC Act, the Commission in completing a determination is required to consider the cost and efficiency factors, as detailed below:

- *the cost of providing the regulated services (Part IV 20.(2e));*
- *the need for greater efficiency in the supply of regulated services to reduce costs to consumers and producers (Part IV 20.(2c));*
- *any arrangements that a person providing the regulated services has entered into for the exercise of its functions by some other person (Part IV 20.(2k)).*

#### 5.1.1 Operating Costs

The setting of taxi fares in the ACT has relied upon the use of a 'taxi cost' index. The index was initially developed by the Taxi Industry Advisory Council, an advisory body to the ACT Government. The index is comprised of a number of cost items associated with the operation of a taxi. It is not intended to provide an estimate of the **actual** cost of operating a taxi in the ACT, but rather seeks to measure the movement in these operating costs over time. To the extent that a taxi operator covers more or less distance than that assumed in the construction of the index, the overall operating costs will differ from those represented in the index. Similarly, the revenue generated by an individual operator will vary depending on the number of hours the taxi is on the road, the ability of the taxi driver to obtain work, the wider economic conditions, and the influence of external factors such as general weather conditions on the demand for taxis.

By not seeking to replicate the actual total costs and revenue outcomes that an average taxi can expect to face, the use of a taxi fare index of the type used in the ACT, avoids the complicated questions of asset value, the number of kilometres travelled in flag fall and non-flag fall mode, and the availability of individual drivers to compete for the available work at any particular time of the day. The composition of the index does seek to give some recognition to the actual breakdown of costs by a taxi travelling an average number of kilometres. It is important that the relative contribution of each of the operating cost components approximate that which is incurred by individual taxis. However, as the index seeks to measure movements on a year on year basis, it is important that the composition of the index remain the same

over time, with any major restructuring of the index requiring an appropriate linking adjustment procedure. There has not been any attempt to alter significantly the composition of the index since its inception over a decade ago.

The form of the taxi index as currently used is that it provides a current period weighted index. Thus, to the extent that there are changes in the relative contribution of individual cost components to the total index, these changes are reflected in the index results.

The submission from the ACT taxi industry through Aerial Taxi Cabs Co-operative Society Limited (Canberra Cabs) summarise the comparative ‘costs’ used in the taxi industry price index. These details are provided in Table 5.1. The index is based upon actual costs for the period 1999/2000, compared to actual costs for the period 1998/99. As noted above, the costs shown in Table 5.1 do not purport to be the actual costs incurred by any individual operator, but rather represent an indicative cost structure.

**Table 5.1: Taxi Industry Prices Index Comparative Cost Table 1999 and 2000**

Item	1999 Costs	2000 Costs	Percent Change
<b>1. Fixed Costs</b>			
1.1 Depreciation	6636	6811	2.64
1.2 Registration costs	5169	5804	12.28
1.3 Driver's licence	22	22	0.00
1.4 Comprehensive insurance	6539	6653	1.74
1.5 Illness and accident insurance	1803	1432	-20.58
1.6 Workers' compensation insurance	1190	843	-29.16
1.7 Superannuation	3528	3755	6.43
1.8 Base fees	<u>10524</u>	<u>11076</u>	<u>5.25</u>
<b>Sub Total</b>	<b>35411</b>	<b>36396</b>	<b>2.78</b>
<b>2. Variable Costs (Non-Labour)</b>			
2.1 Fuel	12204	16524	35.40
2.2 Tyres	1952	1800	-7.79
2.3 Repairs and Maintenance	14279	16439	15.12
2.4 Miscellaneous	<u>2618</u>	<u>2681</u>	<u>2.41</u>
<b>Sub Total</b>	<b>31053</b>	<b>37444</b>	<b>20.58</b>
<b>3. Variable Costs (Labour)</b>			
3.1 Labour	88884	94600	6.43
<b>Total Cost</b>	<b>155348</b>	<b>168440</b>	<b>8.42</b>

Source: Canberra Cabs Submission.

In its submission to the Commission, Canberra Cabs has noted the following changes in the cost components of the index:

- depreciation – increase in costs reflect increased vehicle costs;
- registration – increase reflects increase in Government related registration changes;

- comprehensive insurance – increase reflects the increase in the price of a new vehicle;
- illness and accident insurance – decrease due to a decrease in the average rate of the premium;
- workers' compensation insurance – decrease reflects a competitive move in the market to reduce rates;
- superannuation – increase reflects the increase in wages;
- Aerial Co-operative base fees – increase reflects the change in operating costs for the dispatch of radio controlled vehicles;
- fuel – significant increase reflects increase in LPG prices;
- tyres – decrease reflects a reduction in the manufacturer's retail prices;
- repairs and maintenance – has increased in line with increases in the market for motor vehicle repairs and maintenance activities;
- miscellaneous costs – reflects the increase in the Canberra All Groups CPI;
- labour – increase reflects increase in the Average Weekly Earnings – Full Time Adults (Ordinary Time Earnings) for the ACT as published by the Australian Bureau of Statistics.

The Commission has examined each of the cost components included in the taxi price index. The sources of data have been cross checked to ascertain whether the proposal presented by Canberra Cabs represented a reasonable estimate of the index components.

The major cost increases have been recorded in:

- registration costs;
- fuel;
- repairs and maintenance;
- labour (including superannuation).

Registration cost increases primarily reflect increases in changes introduced by the ACT Government and under the provisions for third party personal insurance which are a compulsory component of registration costs. The proposed increases appear to be consistent with the cost increases that have occurred.

Fuel increases reflect changes in the retail price of LPG over the 12 months 1999/2000. There is evidence that fuel prices have increased considerably over the last 12 months and are likely to continue to increase in the short term. The 35.40 percent is consistent with movement in the retail price of LPG over the 12 month period. Over the same period, retail prices for non leaded petroleum in the ACT has increased by a similar amount. Thus, the Commission has accepted the cost increase that is proposed in this component in the index.

Repairs and maintenance costs are comprised of an extensive list of replacement parts and standard repairs that can be expected to be undertaken over time. The repair and maintenance expenses are based on information obtained from motor vehicle repairers and spare parts outlets around Canberra. Similar suppliers have been used for each year the index is prepared, and thus there is reasonable comparability in the data between years. These repairs and maintenance costs are calculated on the basis of replacement or repairs after a certain number of kilometres. Not all costs are annual, but a portion of these costs is included in the index where the expenditure is required after more than one year.

In checking the calculations prepared by Canberra Cabs, the Commission found some computational errors made in the calculation of the total cost. Essentially Canberra Cabs had incorrectly included twice the value of certain periodic repair costs in the index when in fact these costs would have only been incurred every two years (thus only 50 percent of the cost would have been included in the index for the year 2000).

After making an adjustment, for these computational errors, the total expenditure on repairs and maintenance was reduced from \$16,524 as shown in Table 5.1 to \$15,324. Thus, instead of these costs increasing by over 15 percent as proposed by Canberra Cabs, this cost then grows by 7.32 percent.

Labour costs (including superannuation) have been increased based on the increase in Average Weekly Earnings – Full Time Adults (Ordinary Time Earnings – ACT)<sup>2</sup>. These costs changes have been accepted.

Table 5.2 provides a revised summary of the price index costs after the adjustments outlined above.

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<sup>2</sup> Australian Bureau of Statistics, No 6302.0, November 1999 on November 1998.

**Table 5.2: Taxi Industry Prices Index Amended Comparative Cost Table**

Item	1999 Costs	2000 Costs	Percent Change
<b>1. Fixed Costs</b>			
1.1 Depreciation	6636	6811	2.64
1.2 Registration costs	5169	5804	12.28
1.3 Driver's licence	22	22	0.00
1.4 Comprehensive insurance	6539	6653	1.74
1.5 Illness and accident insurance	1803	1432	-20.58
1.6 Workers' compensation insurance	1190	843	-29.16
1.7 Superannuation	3528	3755	6.43
1.8 Base fees	<u>10524</u>	<u>11076</u>	<u>5.25</u>
<b>Sub Total</b>	<b>35411</b>	<b>36396</b>	<b>2.78</b>
<b>2. Variable Costs (Non-Labour)</b>			
2.1 Fuel	12204	16524	35.40
2.2 Tyres	1952	1800	-7.79
2.3 Repairs and Maintenance	14279	15324	7.32
2.4 Miscellaneous	<u>2618</u>	<u>2681</u>	<u>2.41</u>
<b>Sub Total</b>	<b>31053</b>	<b>36329</b>	<b>16.99</b>
<b>3. Variable Costs (Labour)</b>			
3.1 Labour	88884	94600	6.43
<b>Total Cost</b>	<b>155348</b>	<b>167325</b>	<b>7.71</b>

Source: IPARC analysis.

### 5.1.2 Efficiency Gains

Efficiency gains are included in the taxi industry price index to the extent that there are efficiency savings in the individual cost components. Thus, for example, there are some components of the repairs and maintenance cost category where there have been cost savings since 1999. To the extent that efficiencies occur in suppliers to the taxi industry, these efficiencies are reflected in the index.

However, to the extent that efficiencies arise in the operation of the taxis themselves, these efficiencies are not reflected in the taxi cost index. For example, efficiencies in the location of taxis through better radio and vehicle location technology is not reflected in the index in its present form. Rather, the additional cost of such technology is included in the taxi cost index through the radio costs and taxi base changes which incorporate these new technology costs. To the extent that taxis are more readily able to respond to calls from the general public, there is a benefit that is transferred to taxi users. However, to the extent that taxi operators are able to improve their general profitability through greater operating efficiency, there is no opportunity for these efficiency gains to be passed through to taxi users. In a competitive market in which prices were set by direct competition between taxi operators, these cost saving benefits would ultimately flow through to taxi users.

The Commission is not convinced that the use of a taxi cost index is necessarily the best mechanism for determining prices which reflect efficient operating costs. The Commission recognises the reasons why a cost index of the type used has been

adopted to date. However, the Commission intends to explore further other alternatives or variations to the cost index with the objective of encouraging greater efficiency in the operation of taxis in Canberra and the pass through of efficiency savings in terms of taxi fares.

## **5.2 Consumer Protection**

Under Part IV of the Act, the Commission in completing a determination is required to consider the consumer protection factors as detailed below:

- *the protection of consumers from abuses of monopoly power in terms of prices, pricing policies and standard of regulated services (Part IV 20.(2a));*
- *standards of quality, reliability and safety of the regulated services (Part IV 20.(2b));*
- *the social impacts of the decision (Part IV 20.(2g));*
- *the effect on general price inflation over the medium term (Part IV 20.(2j)).*

### **5.2.1 Pricing**

In determining fares to take effect from 1 July 2000, the Commission has to give consideration to the break up of fares between the various components. These components are:

- flag fall;
- distance related charge;
- booking fee;
- waiting time.

Taxi mileage rates in Canberra are currently structured such that a higher rate applies to travel undertaken after 9pm and prior to 6am. The objective is to encourage taxis to be available at these ‘after hour’ times when there is potentially less demand for taxis. Different mileage rates also apply to multiple hiring of a vehicle, and for passengers using maxi cabs having six or more passengers.

Current changes are summarised in Table 5.3.

**Table 5.3: Current Taxi Charges**

Flag fall		\$2.90
Flag fall (multiple hiring)		\$2.25
Booking fee		60 cents
Waiting time		\$24 per hour (40 cents per minute)
Ordinary hiring		
Rate 1 (6.00am to 9.00pm)		\$1.005 per km
Rate 2 (9.00pm to 6.00am)		\$1.16 per km (15% premium on Rate 1)
Multiple hiring		
Rate 3 (6.00am to 9.00pm)	75% of ordinary mileage rate	{ 75.1 cents per km 86.3 cents per km
Rate 4 (9.00pm to 6.00am)		
Maxi cab hiring (6 passengers or more)		
Rate 5 (6.00am to 9.00pm)	150% of ordinary mileage rate	{ \$1.5075 per km \$1.74 per km
Rate 5 (9.00pm to 6.00am)		

Source: Canberra Cabs.

In seeking an increase in taxi fares in recognition of an increase in operating costs, Canberra Cabs is proposing that the flag fall, radio fee and waiting time charge all remain unchanged. Thus any increase in fares should apply to the distance rate. The way that this rate is determined is to calculate a total fare based on an average distance travelled and including a flag fall, radio fee and waiting time element, and to increase this fare by the proposed percentage cost increase. Essentially the formula works thus:

$$(A + (8.8 \times B) + C + D)r$$

where:

- A is the flag fall, currently \$2.90
- B is the Rate 1 distance fares, currently \$1.005
- C is the waiting time for one minute
- D is the radio fee
- r is the proposed fare increase

The 8.8 average trip kilometres used in the formula is based on observation of the average distance travelled by taxis in Canberra with their meters on. The final fare outcome could be highly sensitive to changes in the average distance travelled used in the fare formula. The 8.8 kilometre average has been used in previous years, and for purposes of adjusting fares from one year to another, the average distance travelled should remain constant whatever the value adopted. From observation the 8.8 kilometre average is not inconsistent with distances travelled by taxis in Canberra when engaged.

Table 5.4 provides a summary calculation of the fare structure assuming an increase of 7.7 percent as outlined in Table 5.2.

**Table 5.4: Possible Fare Structure**

<b>Current Fare Structure</b>	
Flag fall	\$2.90
Kilometre rate – Rate 1	\$1.005 per kilometre
Waiting time	\$24 per hour (40 cents per minute)
Phone booking charge	60 cents
Average distance travelled	8.8 kilometres
Average fare	$\$2.90 + 8.8 \times 1.005 + 40c + 60c = \$12.74$
<b>Proposed New Fare</b>	<b><math>\\$12.74 \times 1.0771 = \\$13.72</math></b>
<b>Fare composition</b>	
Flag fall	\$ 2.90
Waiting time	\$ 0.40
Radio fee	\$ 0.60
Kilometre rate – Rate 1	$\$ \underline{9.82} = \$1.12$ per kilometre
	\$13.72

Source: ICRC analysis.

Adoption of the formula producing a Rate 1 kilometre rate of \$1.12 equates to an increase in the Rate 1 per kilometre rate of 11.4 percent. Commensurate rate adjustments would apply to the other rates. However, the Commission must consider whether or not there should be some adjustment to the other components of the total fare rather than the increase fall totally on the distance component.

The flag fall rate is a fixed charge which theoretically should represent the fixed costs incurred in having taxis available for hire. While not wanting to test whether the current flag fall rate represents an appropriate charge in itself, it is relevant to note the relative flag fall rates as they apply in other States (see Table 5.5).

**Table 5.5: Flag Fall Rates in Other States**

ACT	\$2.90
NSW	\$2.20
Victoria	\$2.60
South Australia	\$2.10/\$4.00
Queensland	\$2.00/\$3.10
Tasmania	\$2.40
Western Australia	\$2.50/\$3.60

Source: Canberra Cabs.

The NSW rate represents a special example where the rate was reduced by \$1 reflecting concerns regarding service standards. In South Australia, Queensland and Western Australia a higher flag fall rate applies for after hours taxi hire. This usually applies between 9pm and 6am.

The flag fall rate in Canberra is already at the higher end of the spectrum by comparison with other States (excluding after hours fares). This does not suggest that the rate in Canberra is inappropriate, but rather serves to highlight the concern within the Canberra taxi industry that any increase in the flag fall rate could discourage

future taxi patronage. With taxi hirings already showing signs of decline in the ACT, the industry's concern is understandable.

The taxi price index does not provide a good indication of what adjustment should be made to the flag fall rate. However, if this was also increased by 2.78 percent which is equivalent to what is called the 'fixed costs' in the index, then in round terms, the flag fall rate could be increased to \$3.00. This would have the result of reducing the per kilometre rate (Rate 1) from \$1.12 per kilometre to \$1.105 per kilometre, or an increase of 9.9 percent on the current rate.

The radio fee is also an area where some change could be made in the charge. The base fees represent 6.6 percent of the total costs calculated by the taxi index and have increased by 5.25 percent in the current index (see Table 5.2). Table 5.6 below provides a comparison with radio fees charged in other States.

**Table 5.6: Radio Fees in Other States**

ACT	\$0.60
NSW	\$1.00
Victoria	\$1.00
South Australia	Nil
Queensland	\$0.80
Tasmania	Nil
Western Australia	Nil

Source: Canberra Cabs.

The radio fee in the ACT at 60 cents is around the average for the industry, but less than in some States where it is as high as \$1.00. If the base fee cost increase shown as 5.25 percent in Table 5.2 was to be adopted, the radio fee could be increased to 63 cents. Again, this would have the effect of making a small difference to the per kilometre rate, although the actual difference is insignificant. However, if the call fee was increased to \$1.00 as in NSW and Victoria, the per kilometre rate increase could be reduced to 6.5 percent.

Waiting time charges in the ACT are commensurate with rates in other States with the exception of NSW where the charge is \$34.80 per hour. Waiting time is a factor of both labour costs and lost productive time. If the labour cost in the taxi cost index is used as a proxy for this cost increase, waiting time could be increased by 6.43 percent (see Table 5.2) to \$25.50 per hour (or 42.5 cents per minute). Again, this would have a marginal impact on the per kilometre rate.

### **5.2.2 GST Impact**

The price outcomes discussed in Section 5.2.1 are exclusive of the impact of the GST on taxi fares. From 1 July 2000, a GST at a rate of 10 percent will apply to the total taxi fare, and this will increase all components of the total fare. The Australian Competition and Consumer Commission (ACCC) has the powers under the *Trade*

*Practices Act 1974* to ensure that any price increase attributed to the introduction of the GST concurs with the Federal Government's objective that the tax is calculated as 10 percent of the cost of the good or service, and that any cost saving achieved by the supplier of the good or service as a result of the removal of other indirect taxes (such as Wholesale Sales Tax) or changes to taxes such as fuel excise, be fully reflected in the net price adjustment. Under an agreement between the ACCC and State jurisdictional regulators including the Independent Competition and Regulatory Commission, the jurisdictional regulators have responsibility for ensuring that the net adjustment in regulated prices set by the jurisdictional regulator, meet the intent of the provisions of Section 75AU of the *Trade Practices Act*.

Queensland Transport has appointed PricewaterhouseCoopers to prepare a methodology for use by the taxi industry for calculating the likely cost savings from the proposed tax savings under the Federal Government's *A New Tax System (ANTS)* package and to calculate the net GST impact. In its submission to the Commission, Canberra Cabs has argued that the net GST inclusive increase, after allowing for cost savings, should be 8.21 percent. The Commission has sought to check these estimates to arrive at an appropriate net GST adjustment for fares. The Commission notes the cost savings estimated by Canberra Cabs are based on the taxi price index results presented in Table 5.1. As previously discussed these contained some arithmetic errors which were corrected in Table 5.2. Thus some modification to these results are warranted.

Upon examining the estimates prepared by Canberra Cabs, the Commission has ascertained that while direct WST savings have been identified, other embedded cost savings from suppliers have not been recognised. Thus the cost savings estimated by the industry require further consideration in order to meet the ACCC guidelines and legislative requirements. The Commission also notes that the main cost savings have been derived from estimates prepared by PricewaterhouseCoopers. The Commission has examined these estimates and is prepared to accept them as the direct WST related cost savings. However, the Commission believes that the PricewaterhouseCoopers model as provided to the taxi industry has not been fully implemented in the submissions from Canberra Cabs. Accordingly the Commission has prepared its own estimates of the additional cost savings which it believes should be included to capture in particular, the embedded cost savings that should be realised in 2000/01.

Table 5.7 provides a summary of the submission on cost savings provided by Canberra Cabs and the adjustments made by the Commission in arriving at an estimate of the likely cost saving. The cost estimates presented in Table 5.7 are based on the taxi cost index as outlined above.

**Table 5.7: Estimated Savings from ANTS Tax Reforms**

Cost Items	2000 Costs <sup>(a)</sup> Estimate	Canberra Cabs Submission		Commission's Revised Estimates	
		% Cost Saving	Estimated Cost	% Cost Saving	Estimated Cost
Depreciation	6,811	-8.5%	6,231	-8.5%	6,231
Registration costs	5,804	-	5,804	-0.9%	5,754
Driver's licence	22	-	22	-	22
Comprehensive insurance	6,653	-	6,653	-1.0%	6,586
Illness and accident insurance	1,432	-	1,432	-1.0%	1,418
Workers' compensation insurance	843	-	843	-1.0%	835
Superannuation	3,755	-	3,755	-	3,755
Base fees	11,076	-	11,076	-0.8%	10,987
Fuel (LPG)	16,524	-	16,524	-2.5%	16,111
Tyres	1,800	-17.0%	1,494	-17.0%	1,494
Repairs and Maintenance	15,324 <sup>(b)</sup>	-11.2%	13,605 <sup>(b)</sup>	-11.2%	13,605
Miscellaneous	2,681	-	2,681	-1.0%	2,654
Labour	94,600	-	94,600	-	94,600
<b>Total</b>	<b>167,325</b>	<b>-1.56%</b>	<b>164,720</b>	<b>-1.96%</b>	<b>164,052</b>

(a) From Table 5.2

(b) Adjusted to reflect arithmetic error in original submission from Canberra Cabs.

Source: Commission analysis.

Adjustments included by the Commission have been:

- an allowance for one percent cost saving on Third Party Personal Insurance costs (under registration costs);
- an allowance of one percent cost saving on Comprehensive Insurance costs, Illness and Accident Insurance costs, and Workers' Compensation costs;
- an allowance of 0.8 percent cost saving on Base Fees (equivalent to a reduction of around 1.6 percent on base costs exclusive of labour);
- an allowance of 2.5 percent cost saving on LPG;
- an allowance of one percent cost saving on miscellaneous charges which are primarily vehicle cleaning and various administrative costs.

The cost saving calculated in Table 5.7 represents a 1.96 percent saving on the taxi industry price index based on the index cost estimates for the 2000. This is equivalent to a net GST price increase of 7.85 percent by comparison to the industry's proposal for a 8.21 percent net increase.

## 5.3 Financial Viability

Under Part IV of the IPARC Act, the Commission in completing a determination is required to consider the financial viability factors as detailed below:

- *an appropriate rate of return on any investment in the regulated industry (Part IV 20.(2d));*
- *the borrowing, capital and cash flow requirements of persons providing regulated services and the need to renew or increase relevant assets in the regulated industry (Part IV 20.(2i)).*

### 5.3.1 Appropriate Rate of Return

Use of the taxi industry price index does not require that an appropriate rate of return be calculated for this industry. Adoption of the price index approach has largely been dictated by the difficulty in assessing an appropriate regulated asset base for this industry. This has the disadvantage of:

- preventing the independent pricing regulator being able to assess the impact of prices decisions on the financial viability of persons providing taxi services taking into account their funding commitments in addition to their taxi running costs;
- limiting the ability of the pricing regulator to ensure there is an appropriate sharing of efficiency benefits between taxi owners/operators and consumers;
- limiting the ability of the prices regulator to adjust prices in accordance with the returns available from competing investment opportunities in the economy.

It is evident from the willingness of new entrants into the taxi industry to pay ever increasing higher prices for taxi plates, that taxi operators who have held plates for many years are making a considerably high return on their initial investment. These high returns reflect the historical cost of the initial investment in the plates by these owners.

This is not necessarily inappropriate, although there has been considerable debate between regulators and more widely throughout the business community, as to whether regulators should assess appropriate financial returns upon the historical cost of the initial investment, or some current cost equivalent. This report is not the appropriate place to debate this issue. However, it is of some concern to the Commission that there is no information available at this time which allows the Commission to form a view on what should be an appropriate rate of return for this industry and what asset valuation should be used in applying this rate of return.

The Commission will be giving further consideration to this matter, and in particular whether it might not be more appropriate to consider a taxi industry prices index which incorporates some estimate of the appropriate return on capital in addition to operating costs and return of capital (depreciation) as is included in the present index used in the ACT.

### **5.3.2 Borrowing, Capital and Cost Flow Requirements**

This issue has largely been addressed under 5.3.1 above.

The Commission invites submissions on the issue of borrowing, capital and cost flow requirements as part of the response to this Draft Direction.

## **5.4 Environmental Issues**

Under Part IV of the IPARC Act, the Commission is also required to consider a number of environmental and demand management issues as detailed below:

- *the principles of ecologically sustainable development referred to in subsection 7(2) of the Territory Owned Corporations Act 1990 as modified by virtue of subsection 4(1) of that Act (Part IV 20.(2f));*
- *consideration of demand management and least cost planning (Part IV 20.(2h)).*

Public transport provides an alternative to the use of private motor vehicles. The Commission has in previous reports<sup>3</sup> highlighted the significant role public transport can play in reducing the number of private motor vehicles on the roads and contributing to improved air quality.

In a recent publication released by the Australian Bureau of Statistics<sup>4</sup> it is reported that almost a third of Canberra residents used public transport during October 1999. Primarily this usage was of ACTION's buses, with school aged children being the largest group to use buses. However, part of this public transport usage was also of taxis in the ACT. Taxis provide an alternative form of public transport, and although they may be not as efficient as buses in the potential to reduce carbon emissions per passenger journey undertaken, they do provide a more environmentally friendly alternative to greater use of private car transport.

Despite these results from the ABS survey, the fact still remains that for both buses and taxis there has been a pattern of declining patronage over recent years. In more recent months, and since June 1999, the taxi industry in the ACT reports that this downward trend which has been evident since the end of 1995, has now shown signs

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<sup>3</sup> IPARC, *ACTION's Bus Fares for 2000/01, Price Direction*, March 2000.

<sup>4</sup> *Usage of Public Transport and Emergency Services*, ABS, Cat No 1303.8.

of improving. The Commission also found that there was some improvement in the usage of ACTION buses in the ACT over the same period (and following the release of Network 99). However, the overall picture is not one of a significant move to public transport. Rather, as noted in the release from ABS on public transport usage, the transport of school children is predominant in these public transport usage statistics.

The Commission notes that the slight improvement in usage of taxis from mid 1999 followed the Commission's decision to allow an increase in average fares of only 2.34 percent from 1 July 1999. For the period commencing 1 July 2000, the taxi industry is seeking an increase in fares of 8.42 percent. In addition, the impact of a 10 percent GST (notwithstanding that there will be some cost savings from the removal of WST and other State and indirect taxes) will result in a considerable increase in fares from 1 July. With inflation in the ACT currently running at around 2.8 percent per annum, the proposal by Canberra Cabs to increase taxi fares in real terms by around 5.5 percent prior to the net GST impact could result in a deterioration of use of this form of public transport. From an ecologically sustainable development perspective, this may not be in the best interest of the ACT and its population.

It is important to note however, that at the same time that operating costs for the taxi industry are rising (and thereby flowing into increased fare rates), many of the underlying operating costs for private motor vehicles are also increasing. This is reflected in increases in fuel costs and increases in motor vehicle repairs and maintenance costs. That these cost impacts may not be fully recognised by the general public (for example, new vehicles come with extended free maintenance warranties, and private vehicle owners can delay repair work on their vehicles whereas taxi owners are required to maintain vehicles at a high standard) could mean that the relative cost impact on private motor vehicle ownership may not be as high as for the taxi industry.

The change in the relative cost of taxi fares by comparison to other forms of public transport and the likely environmental impact should be considered in the context of the likely diversion of passenger journeys from taxis to private motor vehicles. Taxis contribute to only a small proportion of the total passenger movements within the ACT. These passenger movements reflect business usage (for example, travel from office or home to the airport or to other business functions), and day to day convenience travel (for example, transport between home and shopping centres), medical (for example, special transport facilities for people needing to travel between medical practices and home) and recreational use (for example, travel to and from hotels, bars and restaurants). Other factors beyond simply the level of fares will influence the decision to undertake some of this travel (for example, strong enforcement of drink/driving laws, need for special transport to move people requiring medical treatment from their homes to this treatment, and business travel convenience).

The Commission is therefore of the view that while an increase above the current rate of inflation will cause some potential taxi users to seek alternative forms of transport, the overall impact, while still possibly resulting in some further reduction in the number of taxi journeys undertaken, will not contribute to any significant increase in environmental and air quality problems.

## **6. PROPOSED PRICE PATH AND MAXIMUM FARES**

The Commission has been asked to issue a Direction covering:

- the maximum taxi fares for taxi services provided within the ACT, for a period of between three to five years; and
- the method or formula as appropriate which may be used to set this price path.

### **6.1 Price Path**

It is generally agreed in Australian regulatory circles, that some form of incentive based regulation provides a better overall mechanism for setting prices for regulated businesses than an annual determination using some form of cost increase index or indicator. An incentive form of regulation such as a CPI-X price path gives the opportunity for the regulator to set a price path which challenges the regulated industry to achieve some targeted level of efficiency.

This ensures that consumers are able to benefit in the efficiency targets set by the regulator. If the regulated industry is able to do better in terms of its efficiency than the targets set by the regulator, then the industry is able to retain these benefits.

Incentive forms of regulation only work if price paths are set for more than one period. This allows the regulated industry to improve its efficiency over time and provides clear guidance as to what will be the price path over the period concerned.

An annual price determination using a cost index such as the taxi industry cost index, does not allow the regulator to set these forms of incentives for best practice performance in a way that the industry can achieve the targets and possibly better these targets.

Canberra Cabs has not expressed a preference to the Commission on what type of price setting arrangement it would prefer. Submissions from Canberra Cabs have been in the form of these annual cost index model. However, in discussions with Canberra Cabs executives, the Commission has been advised that Canberra Cabs would be willing to consider alternative approaches to price setting.

For the present inquiry, the Commission intends to use the existing taxi cost index to set prices for a 12 month period from 1 July 2000. This will allow time for the industry to consider possible alternative approaches. Also, with the likely impact of the GST and the cost savings arising from the ANTS packaging impacting upon the industry and the pricing model used, the Commission is of the view that it would be better to consider an alternative price determination formula as part of the price review required before 1 July 2001.

However, the Commission does not intend to use the present taxi cost index for prices to be set from 1 July 2001. There will be a need at least to adjust the index for the impact of the GST on prices so that a comparison can be made between costs which exclude the GST in the current index and estimates of costs excluding the GST effect in 2001. In order to achieve this objective, some modelling of GST impacts may be required.

The Commission also proposes exploring with the industry the use of an index which incorporates a provision for funding costs (as discussed under Section 5.3.1. above).

## **6.2 Maximum Prices for 2000/01**

The Commission proposes setting a maximum price path for the 12 month period commencing 1 July 2000 based upon the cost increases as calculated in Table 5.2, that is an increase of 7.71 percent. However, in recognition of the likely cost savings to be achieved from the ANTS package, and in order to meet the ACCC guidelines for the net GST impact to incorporate these cost savings, the percentage increase will be reduced from 7.71 percent to 5.60 percent reflecting the cost savings and revised index results identified in Table 5.7 above.

In applying this cost increase across the various components of a total fare, the Commission is conscious of the need for revised prices which reflect the underlying cost savings from the ANTS package and, after adjustment for cost increases, for prices which can be readily applied by the taxi industry using the metering technology that is currently available. The Commission believes that there is merit in rounding any changes in the radio fee and flag fall elements for the total change, for example, such that they are rounded to the nearest five cents. However, any rounding made in the final changes determined by the Commission should not preclude the application of the appropriate net GST impact (that is, the cost savings from the ANTS package should be seen to have been passed through for each component of the total fare) and the total fare reflect the price increase determined by the Commission.

Accordingly, the Commission has calculated the total fare package on the standard of an average trip of 8.8 kilometres as is normally applied, and then having ensured the pass through of the net GST impact, adjusted the individual components of the total fare such that the total fare increase is consistent with a 7.71 percent increase (prior to ANTS tax savings). The calculations of the revised fare using the formula as presented in Section 5.2.1 are as follows:

Average current fare (see Table 5.4) = \$12.74  
Average fare after Commission endorsed price adjustments = \$12.74 x 1.0771  
= \$13.72  
Average fare after net GST impact = \$13.72 x 1.0785 = \$14.80

Fare composition:

- ♦ Flag fall \$ 3.20
- ♦ Waiting time \$ 0.45
- ♦ Radio fee \$ 0.65
- ♦ Kilometre rate – Rate 1  $\frac{\$10.50}{\$14.80} = \$1.193$  per kilometre

Thus, the Rate 1 fare would be \$1.193 per kilometre. All other rates would be calculated on the basis of the formula as set out in Table 5.3, thus:

Rate 1	\$1.193 per kilometre
Rate 2	\$1.372 per kilometre
Rate 3	\$0.895 per kilometre
Rate 4	\$1.029 per kilometre
Rate 5	\$1.790 per kilometre
Rate 6	\$2.058 per kilometre

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## **Attachment 1: Terms of Reference**

### **Australian Capital Territory**

### **Independent Pricing and Regulatory Commission Act 1997**

### **Reference for Investigation Under Section 15 and Specified Requirements in Relation to Investigation Under Section 16**

**No                      of 1998**

Pursuant to subsection 15(1) of the *Independent Pricing and Regulatory Commission Act 1997* (the Act), I refer to the Independent Pricing and Regulatory Commission (the Commission) the matter of:

- investigating maximum taxi fares for taxi services provided within the ACT, for a period of between three to five years; and
- recommending a method or formula as appropriate which may be used.

Pursuant to subsection 15(3) of the Act, the Commission's investigation will cover taxi fares determined by the Minister for Urban Services under subsection 36(1) of the *Motor Traffic Act 1936*.

Pursuant to subsection 16(1) of the Act, I specify the following requirements in relation to the investigation:

#### **Matters to be Considered**

The investigation should take into account those matters specified in subsection 20(2) of the Act.

The investigation should consider submissions from the public or any other specified person or body as required, including the submission for increased taxi fares prepared by Aerial Taxis.

#### **Outcome**

The outcome of the investigation will form the basis of a report and recommending to the Minister for Urban Services a method or formula, as appropriate, which will be used in the determination of maximum taxi fares under subsection 36(1) of the *Motor Traffic Act 1936*.

**Timeframe**

A final report is to be provided to the Minister for Urban Services by 30 March 1999.

**Brendan Michael Smyth MLA**  
Minister for Urban Services

Dated: 15 June 1998

**Australian Capital Territory**

**Independent Pricing and Regulatory Commission Act 1997**

**Variation to Specified Requirements Under Section 16  
in Relation to Investigation**

**No                      of 1998**

Pursuant to subsection 16(1) and to paragraph 16(2) of the *Independent Pricing and Regulatory Commission Act 1997*, I vary the requirements specified by me by instrument dated 15 June 1998, in relation to the conduct of the investigation referred to the Independent Pricing and Regulatory Commission by that instrument, as follows:

**Timeframe**

A final report is to be provided to the Minister for Urban Services by 30 March 2000.

**Brendan Michael Smyth**  
Minister for Urban Services

Dated: 22 December 1998

**Explanatory Statement**

**Independent Pricing and Regulatory Commission Act 1997**

**Variation to Specified Requirements Under Section 16  
Relating to Investigations**

**No                      of 2000**

Pursuant to subsection 16(1) and to paragraph 16(2) of the *Independent Pricing and Regulatory Commission Act 1997*, I vary the requirements specified by my by instrument dated 22 June 1998, in relation to the conduct of the investigation into taxi fares referred to the Independent Pricing and Regulatory Commission by that instrument, as follows:

**Timeframe**

A report is to be provided to the Minister for Urban Services by 28 April 2000.

**Brendan Michael Smyth**  
Minister for Urban Services

Dated: