

# **ISSUES PAPER**

## **Determination of prices for taxi services**

**November 2001**



**INDEPENDENT COMPETITION AND REGULATORY COMMISSION**



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COMMISSION**

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## **Submissions**

Public involvement is an important element of the Commission's processes. The Commission therefore invites submissions from interested parties to all of its investigations.

Submissions should have regard to the specific issues that have been raised, although additional issues that you feel are relevant may also be canvassed. Submissions should be made in writing and, if they exceed 15 pages in length, should also be provided on computer disk in word processor, PDF or spreadsheet format.

## **Confidentiality**

Special reference must be made to any issues in submissions for which confidential treatment is sought and all confidential parts of submissions must be clearly marked. *However, it is important to note that confidentiality cannot be guaranteed as the Freedom of Information Act and section 44 of the Independent Competition and Regulatory Commission Act provide measures for possible public access to certain documents.*

## **Public access to submissions**

All submissions that are not subject to confidentiality will be made available for public inspection at the Commission's offices immediately after registration by the Commission and also via the Commission's website. Transcriptions of public hearings will also be available.

## **Public information about the Commission's activities**

A range of information about the role and current activities of the Commission, including copies of latest reports and submissions can be found on the Commission's website at [www.icrc.act.gov.au](http://www.icrc.act.gov.au)

**The Commission is headed by:**

**Mr Paul Baxter**

***Submissions on this review should be received no later than 4 February 2002.***

***Comments or inquiries regarding this review should be directed to:***

***Ian Primrose ☎ 02 6205 0799  
Nicholas Hague ☎ 02 9290 8494***

**Independent Competition and Regulatory Commission**

Level 7, 197 London Circuit, Canberra ACT 2600

☎ 02 6205 0799 Fax 02 6207 5887

**All correspondence to: GPO Box 975, Civic Square, ACT 2608**

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## **1 INTRODUCTION**

The Independent Competition and Regulatory Commission is a statutory body set up to regulate prices, access and other matters in relation to regulated industries and to investigate competitive neutrality complaints and government-regulated activities.

The Commission's objectives are to:

- promote effective competition in the interests of consumers
- facilitate an appropriate balance between efficiency and environmental and social considerations
- ensure non-discriminatory access to monopoly and near-monopoly infrastructure.

The Commission operates in a way that is open to industry, members of the Legislative Assembly and the community at large. The Commission's mandate is both to inquire into issues in a publicly accountable and publicly conducted way, and to report its findings and advice publicly. To this end, the Commission encourages public submissions to its inquiries.

The Minister for Urban Services has asked the Independent Competition and Regulatory Commission to conduct an investigation into the determination of prices for taxi services within the Territory. In particular, the investigation is to set fares for a period of two years from 1 July 2002, further develop and refine the new costing and pricing model constructed by the Commission, and address matters referred to in section 20 of the *Independent Pricing and Regulatory Commission Act 1997* (see attachment 1 for the full Terms of Reference).

The indicative timetable for this review is:

<b>Event</b>	<b>Date</b>
release of issues paper	19 November 2001
submissions due on issues paper	4 February 2002
release of draft report	March 2002
submissions due on draft report	April 2002
release of final report	May 2002

The Commission invites interested parties to make submissions to this review. This issues paper provides some background information and highlights some issues the Commission will be considering. Submissions may address these issues, however, the content of this issues paper is not meant to limit the areas that submissions may wish to address. **Submissions to this review should reach the Commission no later than 4 February 2002.**

## **2 PREVIOUS REVIEWS BY THE COMMISSION**

The Commission has previously conducted two reviews of ACT taxi fares. Each of these reviews set fares for a one year period, for 2000/01 and 2001/02 respectively. As highlighted in both the Commission's reports, the setting of taxi fares in the ACT has relied on the use of a 'taxi cost' index. This 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 attempts to measure the movement in these operating costs over time.

The Commission raised a number of concerns with the taxi cost index. While the cost index may be useful in passing on efficiencies associated with inputs purchased in providing a taxi service, eg spare parts and repair work, efficiencies possible and/or achieved **within** the actual operation of the taxi industry are not properly recognised in the index. For example, such efficiencies may arise through better radio and vehicle location technology.

Further, the cost structure behind the index is that which existed when the index was originally constructed. That is, the index reflects a cost structure for a taxi of around 10 years ago. It is possible that the cost structure has changed such that use of the current index, and the share it implies between different cost components, is inappropriate.

The Commission has been concerned that the methodology used to set taxi fares should promote the efficient operation of taxi services, and ensure that efficiency gains are appropriately shared with the customer.

To this end, in its last taxi fare review the Commission developed a new taxi costing and pricing model for the ACT.

### **3 TAXI COSTING AND PRICING MODEL**

The new costing and pricing model developed by the Commission essentially provides a profit and loss statement for a typical taxi operation in the ACT, from the perspective of the taxi owner. In its last review, the Commission set the starting point for the costing and pricing model, with a view to applying the model in later fare determinations. The table over illustrates the costing and pricing model.

The model relates to a single vehicle operating for 206,000km (7,150 driver hours) per year. Two sub-models have been developed. One assumes the owner drives 55 hours per week and also sub-contracts to bailee drivers 88 hours per week. The other assumes that bailee drivers cover all hours. Operations are for 50 weeks per year. It is assumed that the hourly costs for bailee drivers equate to their current average earnings, which are 50 per cent of their gross takings. A surplus under the model suggests that taxi fares should fall.

The variables and assumptions used in developing the costing and pricing model came about through discussions with Canberra Cabs. Obviously, there were some areas where the Commission and Canberra Cabs differed as to the appropriate inputs. However, the Commission's process of developing the new model was open to public consultation, and where differences existed, the Commission's position has been fully explained. Greater detail on the model is available in the Commission's previous taxi fare report.<sup>1</sup>

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<sup>1</sup> Independent Competition and Regulatory Commission, *Taxi fares for 1 July 2001 – 30 June 2003*, Final report, May 2001.

**Table 3.1: ACT taxi costing and pricing model**

	Annual cost – January 2001	
	Owner-driver + bailee drivers	Bailee drivers only
<b>REVENUES</b>		
Gross takings	163,493	163,493
Non-fare income	3,895	3,895
<b>Total Revenue</b>	<b>167,388</b>	<b>167,388</b>
<b>OPERATING EXPENSES</b>		
<b>Fixed Costs</b>		
Vehicle capital costs	6,732	6,732
Vehicle registration costs	6,757	6,757
Driver licence & medical	183	183
Driver safety levy	420	420
Safety camera	600	600
Comprehensive insurance	4,866	4,866
Demurrage Insurance	300	300
Network fees	11,854	11,854
Uniforms	505	505
Office/miscellaneous expenses	2,205	2,205
Sub total	<b>34,422</b>	<b>34,422</b>
<b>Variable Costs: Non-labour</b>		
Fuel	19,700	19,700
Tyres	1,831	1,831
Car washing	1,136	1,136
Repairs and maintenance	17,282	17,282
Sub total	<b>39,949</b>	<b>39,949</b>
<b>Variable Costs: Driver labour</b>		
Driver payments (bailee drivers)	50,306	81,747
Workers compensation insurance (bailee drivers)	1,819	2,920
Illness/accident insurance (owner driver)	1,817	-
Sub total	<b>53,942</b>	<b>84,667</b>
<b>Total Operating Expenses</b>	<b>128,313</b>	<b>159,038</b>
<b>Gross Surplus (Rev-Op Exp)</b>	<b>39,075</b>	<b>8,350</b>
Return on owner-driver labour <sup>1</sup>	<b>33,156</b>	-
Surplus after return on labour, ie net surplus	<b>5,919</b>	<b>8,350</b>

1. Based on same earnings rate/hour as bailee drivers.

At a minimum, the Commission is expecting Canberra Cabs to submit a version of the new costing and pricing model updated for current revenues and costs, plus forecasts of future values such that a two year price path may be implemented. In this review, the Commission will also consider whether the model requires further development and refinement. Canberra Cabs, and other stakeholders, are welcome to comment on such issues.

The Commission would also like to request information and input from Yellow Cabs (Canberra) Pty Ltd. Subject to the views of the incoming ACT Government, Yellow Cabs is to be granted a licence to operate a second taxi network and booking service in the ACT, and will provide an important benchmark on the costs of Canberra Cabs.

The Commission invites comments on the new costing and pricing model for ACT taxis, on any further developments and refinements that may be warranted, and on the quantum of figures that should be contained in the model.

### **3.1 Plate values**

The terms of reference for this review requires the Commission to further develop and refine the costing and pricing model, and 'make provisions, where appropriate, for return on investment...'.

The return on a taxi owners 'investment' can be considered in a number of ways. Firstly, there is the return on the taxi owner's time involved in driving the taxi and managing the taxi operation. These factors have been explicitly captured in the costing and pricing model.

More contentious is the issue of plate values, and whether a return on plate values (or similarly, taxi plate leasing costs) should be included in a fare setting model. The Commission considered this issue during the course of its last review. Following stakeholder consultation at that time, it was determined that plate values would not form a component of the costing and pricing model.

The Commission invites comment on whether this position should be altered. It notes that a recent decision by the Independent Pricing and Regulatory Tribunal of NSW included plate values in the cost index approach to setting taxi fares in NSW.

The Commission invites comments on whether plate values should be accounted for in the costing and pricing model for setting taxi fares, and if so, the method by which it should be included.

### **3.2 Network fees**

The Commission had some concern over the level of network fees quoted by Canberra Cabs at the time of the last taxi fare review. At \$11,854 per taxi per annum, this figure was relatively high compared to interstate costs. Further, the Commission noted that it would be reasonably expected that competition at the network level would lead to reductions in ACT network fees.

The Commission is aware that a second network licence may be granted to Yellow Cabs. Yellow Cabs has indicated that its network fees will be around 30 per cent lower than those offered by Canberra Cabs.

The Commission will review closely the quantum of network fees quoted by Canberra Cabs, and will seek additional information from Yellow Cabs (if granted a licence) during the course of this review.

The Commission invites comments on the level of network fees in the ACT.

### **3.3 Other cost items**

The Commission has been highly reliant on Canberra Cabs for cost, revenue and operational information given its historical monopoly status in the ACT. As noted above, Yellow Cabs may be granted a licence to operate a second taxi network/booking service in the ACT. If this eventuates, the Commission views Yellow Cabs as a useful source of information on efficiency savings that may be achievable for some cost items. Over time, the Commission envisages that Yellow Cabs would be able to provide other useful information on other items such as revenue and operational statistics.

As with network fees, the Commission is aware that Yellow Cabs has indicated that cost savings relative to belonging to Canberra Cabs are available for those taxi operators that change to the Yellow Cabs' network.

The Commission invites comments on the level of all cost items contained within the costing and pricing model, and the level of costs charged by/associated with Canberra Cabs.

## **4 FARE STRUCTURE AND MAXIMUM FARES FOR 2000/01**

In its last review of taxi fares released in May 2001, the Commission set maximum taxi fares for the year 2001/02. In this current investigation, the Commission has been asked to establish maximum fares for a two year period from 1 July 2002.

The following table illustrates the existing fare structure and maximum fares for taxis in the ACT:

**Table 4.1 Taxi fares for 2001/02**

<b>Description</b>	<b>Rate</b>
Flag fall	\$3.20
Flag fall – multiple hiring	\$2.40
Flag fall – maxi cab hiring	\$4.80
Booking fee	\$0.65
Waiting time	\$28.50 per hour (47.5 cents per minute)
Ordinary hiring	
– rate 1 (6am to 9pm)	\$1.282 per km
– rate 2 (9pm to 6am)	\$1.474 per km
Multiple hiring	
– rate 3 (6am to 9pm)	\$0.930 per km
– rate 4 (9pm to 6am)	\$1.074 per km
Maxi cab hiring (6 passengers or more)	
– rate 5 (6am to 9pm)	\$1.987 per km
– rate 6 (9pm to 6am)	\$2.275 per km

As the table shows, taxi fares are distinguished by the nature of the hire (ie ordinary, multiple or maxi cab) and time of day. A similar fare structure is generally found in other cities in Australia and internationally.

Within this general fare structure, differences may occur in regard to varying flag fall rates for day or night hire, and classification of 'day' and 'night' (ie the actual times within which day and night are classified) for example.

One fare structure issue that the Commission attempted to explore during its last review was the differential between day rates and night rates. As the table above shows, the night rate is around 15 per cent higher than the day rate, with that differential reflected solely through the per kilometre charge.

The Commission considers that variable costs would not differ significantly between day and night time operations. For this reason, it would be more appropriate for any differential between day and night rates to be reflected through the flagfall, rather than the kilometre rate. During the last review this issue was discussed with Canberra Cabs, which stated that a standard distance charge irrespective of time of day would act as a disincentive for taxis to accept longer trips.

The Commission was not persuaded by this argument, and has been presented with little empirical evidence to suggest this is the case. In its last review the Commission put the industry on notice that it would look to cite independent data on taxi trips at the time of the next taxi fare review. To this end, the Commission wrote that it 'would encourage the ACT Department of Urban Services and/or the taxi industry to commission an independent survey of taxi trips to establish the average trip length, the distribution of trips around this average, and differences in trip distance depending on time of day'.<sup>2</sup>

As previously noted by the Commission, the fare structure within the ACT is generally consistent with that in other parts of Australia. However, changing the ACT fare structure, eg applying the day/night differential to the fixed charge rather than the kilometre charge, would still leave the structure generally consistent with other states in Australia. The Commission is interested in options for changing the fare structure.

The Commission invites comments on the structure of taxi fares and calls for information to be submitted on average trip length, the distribution of trips around this average, and differences in trip distance depending on time of day.

## **5 COMPETITION POLICY**

The Commission's review of ACT taxi fares is required to take into account 'the degree of competition within the industry and the way in which that may affect the efficiency of the industry'. This was also considered by the Commission in its previous review of ACT taxi fares.

At a meeting of the Council of Australian Governments in April 1995, the Heads of Government signed an agreement to implement the National Competition Policy reform

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<sup>2</sup> Independent Competition and Regulatory Commission, *Taxi fares for 1 July 2001 – 30 June 2003*, Final report, May 2001, p vi.

package. The purpose of the reforms was to remove unnecessary barriers to trade and encourage greater competition within Australia.

Under the reform package, all the Australian Governments have agreed to review and reform their legislation in accordance with the general principle that legislation should not restrict competition unless it can be demonstrated that the benefits of the restriction outweigh the costs to the community as a whole, and the objectives of the legislation can be achieved only by restricting competition.

In this regard, the Commission notes the review conducted by Freehills Regulatory Group on the ACT taxi and hire car industries.<sup>3</sup> The review found that the ACT legislation restricts competition by constraining the supply of licences and through fare regulation. The review also considered the taxi booking/network services market, concluding that the legislation may contribute to Aerial Taxi Cabs Co-operative Society Limited's (Canberra Cabs) monopoly in this market.

Freehills found that the greatest impact on competition was caused by constraints on supply. It found that the licence quota restrictions do not address legislative objectives and impose substantial costs on consumers and potentially on other participants in the industry such as drivers.<sup>4</sup>

The ACT Government has responded to the review, deciding to implement a transitional approach to licensing. Ten wheelchair accessible taxi licences were immediately released, with the Government also moving to strengthen the enforcement of these licences, particularly in giving priority for passengers in wheelchairs.

The ACT Government decided not to release additional standard taxi licences, stating that its surveys indicate that the community is generally satisfied with the performance of the taxi service. These arrangements are to be re-examined before June 2002 to ensure community needs are being met and the industry remains competitive and viable.<sup>5</sup>

In regard to the ACT Government's response, the National Competition Council has stated that the ACT needs to make significant further reform progress in relation to taxi industry regulation.<sup>6</sup> A failure to progress reform is likely to be regarded as a substantial failure to comply with national competition policy obligations. This could impact on the level of national competition policy payments granted to the ACT Government.

The Commission will consider again the state of competition present in the ACT taxi industry. In particular it will focus on developments since its last review and the approach of the ACT Government to these issues.

Beyond the licensing/quota system applied to taxi numbers in the ACT, there are a range of other competitive issues that the Commission wishes to consider during this review. Key

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<sup>3</sup> Freehills Regulatory Group, *National Competition Policy Review of ACT Taxi and Hire Car Legislation*, Final Report, Prepared for ACT Department of Urban Services, March 2000.

<sup>4</sup> *Ibid*, p 1.

<sup>5</sup> Brendan Smyth MLA, Deputy Chief Minister, Minister for Urban Services, Media Release, 15 November 2000.

<sup>6</sup> The National Competition Council is a federal statutory authority, functioning as an independent advisory body for all governments on the implementation of national competition policy. It is the NCC's task to assess progress on meeting the national competition policy reform agenda.

among these are the introduction of a second network operator, and developments in regard to cross-border restrictions between the ACT and Queanbeyan.

The Commission invites comments on the degree of competition within the ACT taxi industry, the way in which this may affect the efficiency of the industry, and related issues.

## **6 SECTION 20 OF THE ACT**

The Terms of Reference for this review requires the Commission to take into account matters referred to in section 20 of the Act. The following reproduces section 20(2) of the *Independent Competition and Regulatory Commission Act 1997*:

- (a) the protection of consumers from abuses of monopoly power in terms of prices, pricing policies (including policies relating to the level or structure of prices for services) and standard of regulated services;
- (b) standards of quality, reliability and safety of the regulated services;
- (c) the need for greater efficiency in the supply of regulated services to reduce costs to consumers and taxpayers;
- (d) an appropriate rate of return on any investment in the regulated industry;
- (e) the cost of providing the regulated services;
- (f) 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) that Act;
- (g) the social impacts of the decision;
- (h) considerations of demand management and least cost planning;
- (i) 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;
- (j) the effect on general price inflation over the medium term; and
- (k) any arrangements that a person providing regulated services has entered into for the exercise of its functions by some other person.

The Commission is required to take into account a wide range of matters in making its price direction. This ensures that an appropriate balance of interests is considered, eg both the returns to the service provider and also the protection of consumers from excessive prices.

During the last review, issues concerning service quality, provision of information, and the meeting of licence conditions arose. Each of these essentially relate back to issues of the protection of consumers from the abuse of monopoly power in terms of standard of regulated services (clause 20(2)(a)), and standards of quality of the regulated services (item 20(2)(b)). Specific issues that arose during the course of the last review included:

- the need for the service quality indicators in the memorandum of understanding between the ACT Government and Canberra Cabs to be reviewed, with particular attention paid to tightening peak period waiting time requirements
- improved monitoring of wheelchair accessible taxi service standards be implemented, with appropriate sanctions imposed where licence conditions are not met

## **Determination of prices for taxi services**

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- administrative action required of Canberra Cabs by the memorandum of understanding, eg independent audit or quarterly reports, be properly enforced and/or reviewed.

The Commission invites comments on matters referred to in section 20 of the *Independent Competition and Regulatory Commission Act 1997*.



## 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

#### *Reference for Investigation Under Section 15*

Pursuant to subsection 15(1) of the Act, I direct the Independent Competition and Regulatory Commission (the "Commission") to conduct an investigation into the determination of prices for Taxi services within the Territory from 1 July 2002 addressing the following:

1. to further develop and refine the new costing and pricing model constructed by the Commission to determine prices (fares) for taxi services to provide a reliable and sustainable service for the period of the determination for both the industry and consumers. The costing and pricing model should address deficiencies within the existing taxi cost index and make provisions, where appropriate, for return on investment and efficiency gains through technology
2. the recommended maximum fares for the regulated taxi services for a period of two years from 1 July 2002.

Without restricting the Commission in reaching a determination on those matters listed in items 1 and 2 above the Commission is to take into account:

- a) the degree of competition within the industry and the way in which that may affect the efficiency of the industry; and
- b) the matters referred to in Section 20 of the Act.

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

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

- the Commission in conducting its investigation into the determination of fares shall determine a price path capable of being applied over a period of 2 years
- the final report in relation to determined taxi fares for the period 1 July 2002 to 30 June 2004 is to be provided to the Minister of Urban Services by 30 May 2002;

Dated this 6<sup>th</sup> day of September 2001

BRENDAN SMYTH  
MINISTER FOR URBAN SERVICES