

DRAFT REPORT

**Taxi Fares for
1 July 2001 – 30 June 2003**

APRIL 2001



**INDEPENDENT COMPETITION AND REGULATORY
COMMISSION**

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FOREWORD

This is the Commission's draft report on pricing of taxi services for the period from 1 July 2001 to 30 June 2003. The Commission is releasing this draft report as required by section 18 of the *Independent Competition and Regulatory Commission Act 1997*. The Act provides that before a final report on an industry reference is given to the referring authority, a draft report shall be published and submissions invited upon the matters in it. The Act also provides that interested persons may make submissions to the Commission on the draft report within a period of not less than twenty working days.

In its last determination the Commission expressed concern about the effectiveness of the method used to determine taxi fares and indicated that in the course of this inquiry it would want to consider an effective alternative pricing method.

The reference for this inquiry has directed the Commission's attention to matters including recommending a methodology to determine prices that would provide a sustainable price path over the determination period and maximum fares to apply during the period. The Commission was also directed to take into account the degree of competition in the industry and the way that impacted upon efficiency and the matters in section 20 of the Act.

The Commission has made a draft determination on fare levels and has recommended that service quality indicators in the Memorandum of Understanding be reviewed, that there be improved monitoring of WAT service standards, and that the standards be properly enforced. Importantly, the Commission has considered and made recommendations about the continuation of the licence quota arrangements that have been an historical part of the regulation of the taxi industry and other competition policy issues with a view to the long term efficiency of the industry and the interests of consumers.

The Commission proposes that there be no change in taxi fares in 2001-02. The industry had proposed a 7.8 per cent increase in fares. It is important to note that the Commission's draft determination reflects the outcome from a rebasing of the fare determination model. The approach adopted by the Commission has been to project the anticipated cost of providing a taxi service, and to set fares at a level reflecting those costs of providing the service. This represents a different approach to the previous method of setting fares, which had simply applied a cost adjustment mechanism to fare levels used in the previous period. The Commission expects that in the consultation period a number of issues relating to this new model for setting fares will be raised by interested parties, with the potential for some modification of the draft decision in the context of the final report. Accordingly the Commission invites comments on this current draft.

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Submissions on this Draft Decision should be received no later than 3 May 2001.

Submissions

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

Submissions must be made in writing and should refer to relevant ICRC reports and specific issues raised. Whilst there is no standard format for submissions, if they exceed 15 pages in length, they should be provided in hard copy as well as on computer disk in either 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 Pricing 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.

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EXECUTIVE SUMMARY

This executive summary is provided to assist interested parties and other readers of the Commission's detailed report on its draft decision. It summarises the information considered by the Commission, the analysis applied, and the Commission's decision. The summary neither substitutes for, nor forms any part, of the Commission's detailed report.

1 INTRODUCTION

The Minister for Urban Services has requested the Commission to conduct an investigation into the determination of prices for taxi services within the Australian Capital Territory (ACT). The terms of reference establish the tasks to be undertaken by the Commission, and the matters to which it is to give consideration. In particular, under the terms of reference the Commission is required to address:

- the methodology for determining prices, and to recommend maximum taxi fares for a two year period from 1 July 2001
- matters referred to in section 20 of the *Independent Pricing and Regulatory Commission Act 1997*.

2 STATUTORY REQUIREMENTS AND REGULATED SERVICES

The terms of reference for this review require the Commission to take into account matters referred to in section 20 of the Act. In setting maximum prices, the Commission is required to take into account a wide range of matters. 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. The terms of reference identify 'prices for taxi services within the Territory' as the specified regulated service.

PROPOSED MAXIMUM FARES

Recommendation 1 – Maximum fares

The Commission recommends that there be no change to the level of maximum taxi fares from 1 July 2001 – 30 June 2002.

3 INDUSTRY COSTS AND EFFICIENCIES

The setting of taxi fares in the ACT has relied on the use of a 'taxi cost' index. Developed in 1989, the index has been used since as the basis for determining **changes** in taxi fares. ACT taxi fares have never been rigorously 'base-lined' against actual costs; at the introduction of the taxi index, fares were adjusted on a 'reasonableness' basis, and subsequently have been adjusted using the model. Canberra Cabs submits that if the existing cost index is applied, the appropriate fare increase should be 7.81 per cent.

3.1 Appraisal of existing taxi cost index

The Commission has identified major cost areas/issues which it considers the current index model is significantly deficient in reflecting typical taxi industry costs in the ACT:

1. vehicle capital (item 1)
 - current costs over-estimate average vehicle depreciation. Based exclusively on the costs of new vehicles with a functional life of four years, they ignore the mix of vehicles in the fleet and the range of years for which each are used
 - current costs are understated to the extent that they ignore any interest charges on vehicle capital (as most owners lease vehicles these are real financial costs)
2. fuel (item 10)
 - costs are based on an average vehicle travelling 180,000 km pa, whereas the current 'typical' estimate is 206,000 km pa
 - costs are based on LPG consumption of 5.0 km per litre, whereas the current 'typical' estimate is 5.5 km per litre
3. hirings per car
 - in its submission Canberra Cabs indicates that the number of average hirings per car in 2000 was 11,708. This represents a 6 per cent reduction on the corresponding 1999 figure. Given reduced business activity associated with the Olympic Games, the Commission considers a more reasonable annual estimate to be 12,145, which represents a 2.5 per cent reduction on the 1999 figure
4. tyres, repairs and maintenance (items 11, 12)
 - costs are based on 180,000 km pa, whereas the current typical estimate is 206,000 km pa
5. driver labour (item 14)
 - costs (including superannuation and workers compensation) are \$30,000 - \$35,000 per annum too high relative to actual earnings of ACT taxi drivers
 - this item is the largest single contributor to the cost index, representing 55 per cent of total costs. Consequently, it has by far the greatest (absolute) divergence from actual earnings by taxi drivers, with the divergence accounting for 15 - 20 per cent of total costs.

In addition to the above, the current taxi cost index model does not include any allowance for the opportunity cost relating to the cost of taxi plates. The Commission notes the industry's view that the cost index deliberately excludes any consideration of the return on plates and that the fares themselves are not designed to provide any investment return.

3.2 Development of new costing and pricing model

The Commission has constructed a costing and pricing model which encompasses a more realistic treatment of labour costs, and facilitates assessment of the impact of a nominated return on taxi plates.

The model essentially provides a profit and loss statement for a typical taxi operation in the ACT, from the perspective of the vehicle owner. It relates to a single vehicle operating for 206,000 km (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.¹

The table below provides a summary of model results based on current fares and January 2001 operating expenses.

Proposed ACT taxi pricing model

	Annual cost – January 2001	
	Owner-driver + bailee drivers	Bailee drivers only
REVENUES		
Gross takings	169,595	169,595
Non-fare income	3,895	3,895
Total Revenue	173,490	173,490
OPERATING EXPENSES		
Fixed Costs		
Vehicle capital costs	5,354	5,354
Vehicle registration costs	6,757	6,757
Driver licence & medical	61	-
Safety camera	600	600
Comprehensive insurance	4,410	4,410
Network fees	11,854	11,854
Office/miscellaneous expenses	2,205	2,205
Sub total	31,241	31,180
Variable Costs: Non-labour		
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	39,949	39,949
Variable Costs: Driver Labour		
Driver payments (bailee drivers)	52,183	84,797
Administration labour (bailee drivers)	1,225	1,838
Workers compensation insurance (bailee drivers)	1,884	3,027
Illness/accident insurance (owner-driver)	2,028	-
Sub total	57,320	89,662
Total Operating Expenses	128,510	160,791
Gross Surplus (Rev-Op Exp)	44,980	12,699
Return on owner-driver labour ¹	34,391	-
Surplus after return on labour, ie net surplus	10,589	12,699

1. Based on 58 hours/week, (including 3 hours' administration) 50 weeks pa, \$22.865/2 per hour (ie same rate as earned by bailee drivers).

¹ Additional details on the calculation of profit and loss figures presented in the table over are given in attachment 4.

After allowing for a reasonable return on owner-driver labour (equal to the hourly rate earned by bailee drivers), the owner surplus is about \$10,600 - \$12,700 per annum. This represents a 6 - 7 per cent margin on total revenues. Excluding the opportunity cost of plates, a zero surplus could be obtained if fare revenues were reduced by \$21,200 - \$25,400 per annum (around 12 - 14 per cent), ie twice the owner surplus figure. This assumes that the fall in revenue is brought about through a fall in the average fare level only and that costs/distance travelled remain unchanged. Further, it is assumed that bailee driver payments are reduced pro rata.

3.3 Efficiency

The current taxi cost index model is based on the historical costs of a pre-determined set of inputs, which are adjusted periodically by standard indices. It thus cannot allow for changes in efficiency in the use of inputs (eg fuel consumption) or changes in productivity (eg extent of dead running relative to revenue running). Conversely, increases in costs involved to achieve efficiency/productivity gains may be included in the model.

If applied with proper flexibility the proposed model largely overcomes this problem. The model is designed to reflect the absolute costs and revenues from a typical taxi operation. All inputs should be reviewed on a periodic basis, including the assessment of the impacts on costs and revenues of any changes in efficiency/productivity. In this way the proposed model should reflect the absolute costs and revenues for a typical Canberra taxi operation, including any efficiency/productivity changes.

4 PRICING AND CONSUMER PROTECTION

The protection of consumers from abuse of monopoly power through prices can be achieved most appropriately through a proper determination of costs. Given this approach, the Commission is satisfied that the selected cost items and their values are appropriate for fare setting purposes, and protect consumers from any abuse of monopoly power.

4.1 Plate values/return on capital

On the basis of the Commission's analysis, the surplus available after adjustments for return on owner-driver labour is between \$10,600 and \$12,700. In a conventional profit and loss statement, this surplus would be assumed to cover the return on capital - in this case, the return on the value of the taxi plates. The Commission notes Canberra Cabs' view that neither fares nor the previous cost index has explicitly incorporated a return on capital, and the purchase of taxi plates is driven by a number of considerations.

The Commission considers that if it is appropriate to apply a figure for average gross revenues and a figure for average fixed and variable costs, there is a case for assuming that the derived surplus represents an average return on the value of taxi plates. The Commission believes it is appropriate to apply a cost index model which takes into account the implicit annual return on the investment in taxi plates.

Calculations of the surplus imply an average return on taxi plate capital of 4.2 per cent under current fares and on the basis of a current plate value of \$280,000. Of course, not all current owners of plates paid that amount for their plates. The Commission believes that 4.2 per cent represents a reasonable rate of return on plate values.

4.2 Fare structure

Flagfall v distance rate

The current fare structure applies a differential between day rates (1, 3 and 5) and night rates (2, 4 and 6), with the latter approximately 15 per cent higher to provide an incentive for taxis to be available when the demand is generally lower.² The night rate is around 15 per cent higher than the day rate. These differential rates are reflected solely through the per kilometre charges. Flagfall rates remain the same irrespective of time of day.

The Commission notes that during weekday and weekend nights in the ACT, most of the taxi fleet is connected to the network. This suggests that an additional incentive to operate during these times is not required. On Saturday nights, the proportion of taxis engaged reaches 95 per cent. The current market environment suggests that the majority of taxis are on the road at nights, and they are often engaged. This does not support a flagfall differential, but may be used to support providing additional taxi licences to meet demand.

Multiple hiring and maxi cab rates

Different rates apply for multiple hiring (rates 3 and 4) and for maxi cab hirings (rates 5 and 6). The Commission has received little information concerning the frequency of multiple and maxi cab hirings. The historical convention of having different rates for these services, being 75 and 150 per cent respectively has not been examined.

Peak and off peak rates

Despite the varying fare rates, the structure does not distinguish between peak and off peak demand, particularly during the morning and afternoon weekday peak periods. Information on performance suggests that overall, current peak period waiting time requirements for standard taxis are easily achieved. Outside these times, the 85 per cent target is barely achieved. Whether this suggests a need for differential peak and off peak fares is unclear. A review of performance requirements may be more appropriate.

On the basis of the current supply conditions, most taxis are already available throughout the morning and afternoon peaks. Consequently, under current conditions, any am and pm peak pricing differential would be unlikely to increase the supply of taxis, and waiting times would be remain substantially unchanged.

Standard taxis v WATs

Currently, fares are identical for both standard and wheelchair accessible taxis (WATs), despite vehicle costs for WATs being higher. The Department of Health issues taxi vouchers for disabled passengers, however fares earned by taxi drivers are the same for all types of passengers, even though additional costs are associated with loading and unloading disabled passengers. There may be reasons for additional fixed charges associated with the extra time required to serve WAT passengers.

The Commission considers that the market environment in the ACT suggests the existing fare structure be maintained. The Commission's proposal that there be no change to existing fare levels also suggests that the fare structure should not be altered. Nonetheless, the Commission invites comments on whether to vary the existing fare structure.

² Demand information as presented in chapter 5 indicates that demand falls during weekday nights. However, demand on Saturday nights is relatively high compared to demand during the day.

Recommendation 2 – Fare structure

The Commission recommends that the existing fare structure be maintained, with a review to take place when maximum fares are again considered by the Commission.

4.3 Social impacts

The Commission's preliminary analysis in this draft report suggests that no fare increase is warranted. Thus, this proposal raises no concerns in regard to inflationary effects on individuals and inflation in the ACT.

The Commission notes that the ACT Government runs a taxi subsidy scheme designed to assist people with permanent or temporary disabilities who need to use taxis.

4.4 Price path

The Commission is aware of the need to ensure that its price direction will not be inconsistent with any future decision of the ACT Government regarding the structure of the industry. In particular, any changes which led to increased competition could be expected to lead to lower costs for the same level of demand. A reduced requirement for fare increases, or even reductions in fares, could follow.

In the light of possible changes to industry structure and the introduction of a new cost and pricing model, the Commission is considering whether it is more appropriate to provide only a one year determination. In that case, it would monitor the effects of changes over the next 12 months and be in a better position to issue a medium term direction to take effect from 1 July 2002.

4.5 Proposed maximum fares

Canberra Cabs' submission recommends an overall fare increase of 7.81 per cent. The Commission considers that this proposal is not justified. The Commission notes that if a return of 4.2 per cent on current plate values were accepted, there would be no case for an average increase in fares on the basis of the proposed pricing model.

A return of 4.2 per cent on a plate value of \$280,000 effectively represents a higher return for those who purchased plates at much lower historical values. The current position of Canberra Cabs is that plate values not be reflected in the fare setting methodology. Such an approach would suggest a significant fall in fares. It is indicative of an over recovery of costs through fares, given no allowance for a return on plate values. The Commission is satisfied that this proposal for no change in fares is reasonable and justified.

5 SERVICE QUALITY

The primary justification for regulating the taxi industry is that quality standards would suffer in an unregulated environment. Taxi fares are now formally regulated by the Commission. Other aspects of service quality are covered within a Memorandum of Understanding between the industry and the ACT Government. The ACT Government conducts an annual survey of taxi service quality.

5.1 Memorandum of understanding

On 20 June 1997, a Memorandum of Understanding (MoU) was signed by the ACT Government and Aerial Taxi Cabs Co-operative Limited (ie Canberra Cabs, the operator of the ACT taxi network). In place from 1 July 1997 to 30 June 2002, the MoU covers the services to be provided by Canberra Cabs in respect of a taxi booking service.

Schedule 3 of the MoU sets out performance measures and reporting requirements which Canberra Cabs must meet. Quarterly reports are required from Canberra Cabs covering maximum waiting times and response times.

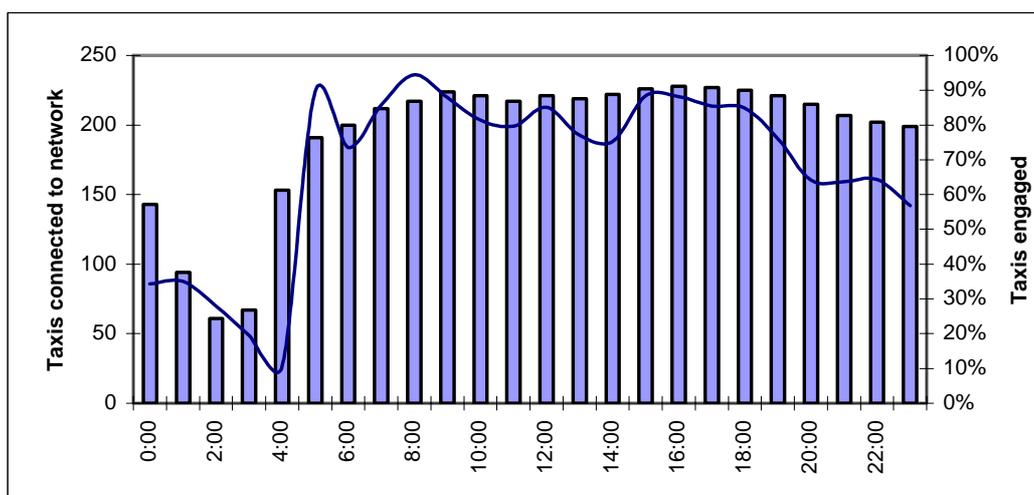
5.2 Passenger demand and waiting times

Demand for taxis varies on a yearly, weekly, and daily basis. Yearly demand shows significant fluctuation. Demand drops significantly over late December and January, with falls also experienced during other school holiday periods. Demand was relatively low in the second half of 2000. This fall was associated with reduced business activity during the Sydney Olympic Games.

Demand differs between weekdays and weekends. On weekdays, there is very low demand in the early hours, with demand peaking around the start and end of the working day. In contrast, on weekends (Saturdays), demand peaks between 6:00pm and 12:00am for telephone bookings, and between 12:00am and 5:00am for rank and hail demand.

The taxi industry/operators have to manage their service provision to meet this varying demand. In periods of high demand, we would expect a relatively higher number of taxis to be connected to the network and engaged. During low demand periods, we would expect to see the opposite. These issues are illustrated in the figures below. The line in each of the figures shows the proportion of taxis connected to the network at that time that are engaged (right hand scale). The columns show the number of taxis connected to the network.

Number of taxis connected to network and % engaged – 9 Nov 2000

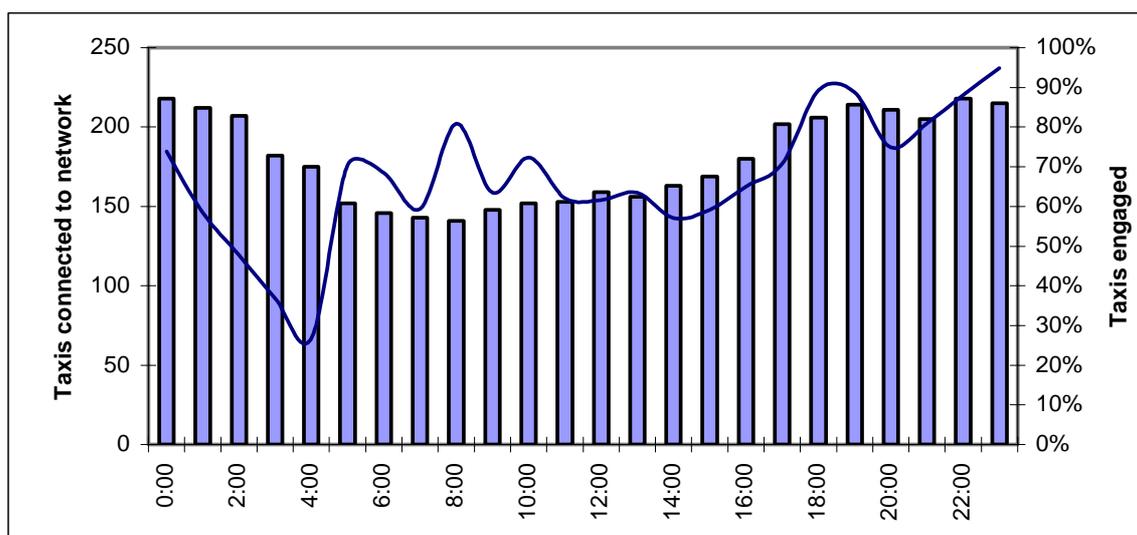


Source: Canberra Cabs.

The number of taxis connected to the network generally varies with daily demand. Relatively low demand corresponds with a relatively low proportion of taxis engaged. For a significant period of the day, the proportion of taxis engaged is over 80 per cent. This is a relatively high figure when compared to taxis in Sydney, where the proportion does not reach 80 per cent even in peak periods. Regardless of different market factors, this suggests that the ACT market has a relatively low number of taxis given the level of demand.

In the figure below for a Saturday, the result for the late evening stands out, with the proportion of taxis engaged reaching 95 per cent. Again, this is a very high result when compared to Sydney.

Number of taxis connected to network and % engaged – 11 Nov 2000



Source: Canberra Cabs.

5.2.1 Waiting and response times

Under the MoU, Canberra Cabs is required to report quarterly on waiting time and response time performance. The MoU requires that Canberra Cabs have its records and quarterly reports independently audited. The Commission is aware that to date this has not occurred, and the ACT Government has not enforced this requirement. The following tables show Canberra Cabs' recent performance:

Waiting times: 3 – 6pm Monday to Friday

MoU requirement	Sep 00	Jun 00	Mar 00	Dec 99
Standard				
85% < 18mins	99.7	99.0	96.3	96.7
95% < 30 mins	98.4	96.0	98.9	98.8
WAT				
85% < 18mins	72.4	66.2	89.5	86.8
95% < 30 mins	87.9	87.8	96.6	93.0

Waiting times: all other times

MoU requirement	Sep 00	Jun 00	Mar 00	Dec 99
Standard				
85% < 10mins	87.7	86.2	86.6	86.6
95% < 20 mins	99.2	98.6	98.9	98.5
WAT				
85% < 10mins	63.0	60.1	81.8	79.3
95% < 20 mins	86.3	84.1	94.7	94.2

Performance for standard taxis generally meets the MoU requirements. Interestingly, performance requirements are barely achieved for 85 per cent of telephone booking customers having to wait less than 10 minutes at 'all other times'. This outcome suggests:

- peak period performance requirements for standard taxis could be tightened
- the indicators do not properly reflect peak periods. The fact that Canberra Cabs' performance requirements are easily met at 'all other times' suggests convergence of performance indicators for current peak and off peak periods may be warranted.

Canberra Cabs performance in relation to WATs is more variable than for standard taxis, and generally does not meet the requirements of the MoU. During peak periods, WAT waiting time targets have not been achieved for the two quarters to September 2000. During 'all other times', Canberra Cabs' failed to meet the requirements of the MoU.

Response times

Generally, response times for standard taxis is 'front loaded' into the less than 5 minutes and 5-10 minutes categories, ie a significant majority of standard taxi customers wait less than 10 minutes for their taxi. For WATs, the degree of 'front loading' is far less compared to standard taxis, ie the average waiting time for WAT users is greater than for standard taxi users. This again suggests that service levels for users of WATs is relatively poor.

5.3 Taxi industry survey

The ACT Government conducts an annual survey of the Canberra taxi industry. The second survey for the year 2000 was released recently. The key findings of the survey are:

- waiting/response times have increased across the board from 1999
- the 85 per cent off peak target (10 minutes) has not been achieved. For standard taxis the response time achieved was 12:53 minutes, and for WATs, 23:08 minutes
- peak period waiting time targets have been achieved for standard taxis and WATs
- off peak waiting time targets for WAT telephone bookings have not been achieved
- drivers of WATs provide a reasonable level of service, although the following matters require attention:
 - the securing of chair and passenger to an adequate standard
 - at what point of the journey the taxi meter should be started
 - defining the service to be provided, eg assistance in gaining access to buildings

- design issue: passengers' ability to see the taxi meter from their seated position.

5.4 Service quality and deregulation

Regulation of the taxi industry is often justified on the grounds that quality standards would suffer in an unregulated environment. If quota restrictions are removed, the relevant government can continue to set service standards, authorise/license networks, operators and drivers, and monitor service provision. Government also retains the power to sanction industry participants where necessary. If strong concerns exist in regard to the effect of deregulation, stringent enforcement of service standards can be applied.

With appropriate safeguards, the Commission considers that the removal of restrictions on the number of taxi licences can promote community benefits.

Recommendation 3 – Service quality

The Commission recommends that:

- service quality indicators in the MoU be reviewed, with particular attention paid to tightening peak period waiting time requirements
- improved monitoring of WAT service standards be implemented, with appropriate sanctions imposed where licence conditions are not met. Government and industry must work together to improve WAT service standards
- administrative actions required of Canberra Cabs by the MoU, eg independent audit of quarterly reports, be properly enforced and/or reviewed.

6 COMPETITION POLICY

The terms of reference require the Commission to consider the 'degree of competition within the industry and the way in which that may affect the efficiency of the industry'. The ACT Government has reviewed legislation relating to the taxi and hire car industries. In fulfilling its own requirements under the terms of reference, the Commission has considered the outcomes of this review and the ACT Government's response to the review.

6.1 Competition and efficiency

Economic theory suggests that in a competitive environment, the interaction between service providers and consumers is likely to produce efficient outcomes (eg fare levels, service quality). In a deregulated market, if the cost of offering a service is greater than the amount consumers are willing to pay, the service will not be offered, or will be withdrawn to avoid the providers of the service making a loss. Furthermore, if a service provider is charging an excessive price, another provider may enter the market, charge a lower price, and win consumers from the previous supplier.

Of course, competition does not work perfectly and may not always be feasible. However, it provides a process whereby misjudgements by producers regarding the cost of production, price or quality of service, may be corrected. Conversely, regulation may maintain excessively high costs or inappropriate services for long periods.

6.2 Freehills report

Independent consultants Freehills Regulatory Group (Freehills) were appointed by the ACT Government to review the ACT's taxi and hire car legislation. Key review findings are:

- licence quota restrictions do not address legislative objectives. They impose substantial costs on consumers and potentially other industry participants, eg drivers
- the provisions create a transfer of wealth from consumers to licence owners and lessees. The quota restrictions inflate the value of licences, reduce potential total hirings and raise fare levels
- regulations which directly address driver, operator and vehicle standards generally have significant benefits in the form of higher consumer, driver and public safety, and in improved quality of service.

Freehills concludes that the removal of taxi quota restrictions is the preferred approach to licence quota reform.

6.3 National Competition Council

The National Competition Council (NCC) is a federal statutory authority which functions as an independent advisory body for all governments regarding the implementation of national competition policy reform. It is the NCC's task to assess progress on meeting the reform agenda. It may recommend that the Federal Treasurer reduce payments to a state or territory where that state or territory has not implemented reform in the public interest.

Taxi licensing has been identified as a key area for concern in the ACT, with the NCC stating a failure to progress reform is likely to be regarded as a substantial failure of compliance with national competition policy objectives.

In order to justify continued regulation, rigorous assessment on public interest grounds must take place, and a net community benefit from continued regulation should exist.

6.4 Matters considered by the Commission

Issues of competition and the taxi industry have been considered widely within Australia over recent years. Reviews of the industry have been conducted at the national level, and also by all state and territory governments. Key conclusions of the reviews include:

- licence quotas have significantly restricted competition
- regulation imposes significant costs on consumers
- regulation has limited service innovation and the pursuit of cost efficiencies by operators in the taxi industry
- licence quotas/entry restrictions should be removed
- licence quotas are not required to meet safety concerns. Such concerns are best addressed directly through regulations supported by appropriate enforcement and sanctions.

The key point of the above is that regulation of the taxi industry has significantly restricted competition. This has had flow on effects in terms of efficiency, and consumers have borne the costs associated with regulation. The Commission considers there are strong arguments to support the removal of competitive restrictions in the taxi industry.

6.4.1 Licence quota restrictions

The ACT Government has stated it prefers a transitional approach to reform. It does not intend to release additional standard taxi licences, and proposes that a further review be conducted prior to June 2002. Ten additional WAT licences have been released.

The Freehills report identifies significant efficiency losses associated with quota restrictions. Competition would remove these losses. The NCC has stated that proposals for a transitional approach to reform be accompanied by rigorous public interest justifications. The Commission recommends that this be done if quota restrictions are to remain in place.

6.4.2 Fare regulation

Freehills recommends that until adequate new entry is established, maximum fare regulation should be maintained. The ACT Government has agreed with this, and proposed that the Commission maintain its role of fare regulation.

The Commission supports continued regulation of the maximum taxi fare. However, it notes that particular care must be taken in setting maximum fares for a market where licence quota restrictions have been removed. The Commission wishes to avoid inappropriate pricing outcomes.

6.4.3 Taxi networks

Freehills recommends that consideration be given to establishing an additional network operator in the ACT. It also recommends that for non dominant networks, minimum response time standards be removed or reduced sufficiently to permit new entry.

The ACT Government has stated that the introduction of an additional network will be invited on similar terms and conditions to those applying to Canberra Cabs. The ACT Government has recently called for tenders for the provision of an additional taxi network service.

The Commission generally supports the introduction of an additional taxi network. However, the Commission has minor concerns with the ACT Government proposal. The full benefits of reform are unlikely to be achieved under a piecemeal approach. In this circumstance, the full benefits from an additional network operator will not be realised in an environment where licence quota restrictions exist.

Also, the Commission would be concerned if a new network operator were not given an adequate opportunity to meet service requirements. During the initial period of its operation, the Commission would encourage the ACT Government to consider the network's performance in the context of supporting the new operator to get established. The Commission is not suggesting service standards be allowed to fall. Rather, that any new operator has an adequate opportunity to meet service standard requirements.

6.4.4 Cross border restrictions

Freehills recommends that the ACT Government work with its NSW counterparts to establish a single taxi regulatory regime for the ACT/Queanbeyan region. The ACT Government has entered into discussions with the NSW Department of Transport.

Notwithstanding the wider issues that will need to be resolved in establishing a single market, the Commission supports this development. It has the potential to increase competition at the network provider level, and between taxi operators. Customers should benefit through the creation of the single market.

6.5 Conclusions and recommendations

Competitive restrictions in the taxi industry have been identified in a number of state/territory and federal reviews of the industry. This includes that of Freehills on the ACT taxi industry. Competitive restrictions affect the efficiency of the industry.

The NCC states that proposals for a transitional approach to reform must be accompanied by rigorous public interest justifications. If quota restrictions are to remain in place, any further review by the ACT Government would need to identify the public interest justifications.

The ACT Government agrees with Freehills' recommendation that until adequate new entry has occurred (following the removal of entry restrictions), maximum fare regulation should be maintained. The Commission also agrees with this approach. However, the Commission notes that particular care needs to be taken when setting maximum fares in a market free of licence quota restrictions.

Recommendation 4 – Fare regulation

The Commission recommends maximum fare regulation be initially maintained when and if licence quota restrictions are removed. If removed, the response of industry should be monitored to determine the requirement for continued maximum fare regulation.

Freehills recommends that consideration be given to establishing an additional network operator in the ACT. The ACT Government has called for tenders to offer such a service. The Commission supports the establishment of another network operator, but has concerns with the approach that may be taken by the ACT Government.

Recommendation 5 – Taxi networks

The Commission recommends that the ACT Government act to encourage the establishment of an additional taxi network service provider. This may be reflected in the assessment of performance against stated requirements.

7 OTHER ISSUES

7.1 Financial viability

The Commission is required to consider factors such as rate of return and borrowing, capital and cash flow requirements when assessing the financial viability of taxi operators. The Commission has considered options for including a rate of return and corresponding capital base in the fare setting methodology.

The borrowing, capital and cash flow requirements of a taxi operator relate closely to the costs of providing the taxi service. These cost issues have been closely considered by the Commission in developing the new fare setting methodology.

7.2 Environmental factors

Public transport provides an alternative to the use of private motor vehicles. The benefits of public transport include reduced congestion and pollution. Generally, these factors have traditionally been couched in regard to public transport options such as rail and buses. Mass transit provides the greatest opportunity to reduce congestion and pollution. Nonetheless, taxis provide an alternative form of public transport, and an environmentally superior alternative to greater use of private motor vehicles.

The Commission is proposing that there be no fare change from 1 July 2001. Obviously, this would have no adverse effects on taxi patronage.

1 INTRODUCTION

The Independent Competition and Regulatory Commission (the Commission) is a statutory body set up to regulate prices, access and other matters relating 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 invites and encourages public submissions to its inquiries.

The Minister for Urban Services has asked the Commission to conduct an investigation into the determination of prices for taxi services within the Australian Capital Territory (ACT). The terms of reference establish the tasks to be undertaken by the Commission, and the matters to which it is to give consideration. In particular, under these terms of reference the Commission is required to address:

- the methodology for determining prices, recommending maximum taxi fares for a two year period from 1 July 2001
- matters referred to in section 20 of the *Independent Pricing and Regulatory Commission Act 1997*.

Attachment 1 contains the full terms of reference for this review.

This is the Commission's second review of taxi fares in the ACT. The Commission previously set maximum taxi fares for the period 1 July 2000 - 30 June 2001.

1.1 Review process

The Commission's review process begins with receipt of terms of reference from the Minister for Urban Services. The terms of reference for this review were signed by the Minister on 6 November 2000, and published in the ACT Government Gazette on 23 November 2000.

In December 2000 the Commission released an issues paper for this review.³ Highlighting key issues for this review, this paper invited submissions from interested parties. The Commission has considered submissions in making its draft decision. A summary of the submission from Canberra Cabs is presented in attachment 2.

³ ICRC, *Determination of prices for taxi services*, Issues paper, December 2000.

Independent Competition and Regulatory Commission

In keeping with the Commission's approach of engaging in public consultation, the draft decision is made available for public comment. Submissions commenting on this draft decision should be received by the Commission by close of business, 3 May 2001. The Commission will issue a final decision by 30 May 2001.

Submissions in respect of this draft decision should be forwarded to:

Paul Baxter
Senior Commissioner
Independent Competition and Regulatory Commission
GPO Box 975
Civic Square ACT 2608

by 3 May 2001

2 STATUTORY REQUIREMENTS AND REGULATED SERVICES

The terms of reference for this review require the Commission to take into account matters referred to in section 20 of the Act. The following reproduces section 20(2) of the *Independent Pricing 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 approach ensures that an appropriate balance of interests is considered, in particular returns to the service provider and protection of consumers from excessive prices.

These matters have been considered by the Commission in making its draft decision. Where appropriate, how the Commission has considered a particular matter is discussed within this report.

The terms of reference issued by the Minister for Urban Services identify 'prices for taxi services within the Territory' as the specified regulated service. Before the Commission's first review into taxi fares, the Minister set fares and the industry made submissions to the Minister for fare changes.

3 INDUSTRY COSTS AND EFFICIENCIES

Under section 20 of the *Independent Pricing and Regulatory Commission Act 1997*, the Commission is required to consider a range of factors relating to industry costs and efficiencies:

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

3.1 Conclusions

The Commission has considered cost proposals submitted by Canberra Cabs. Based on the existing cost index, the Canberra Cabs submission proposes a fare increase of 7.81 per cent. This index was constructed in 1989 with a view to applying appropriate annual percentage movements to individual cost components. It did not purport to reflect **actual** costs at that time. In 1989 fares were assumed to reflect actual costs.

The Commission has identified a number of issues arising from the Canberra Cabs submission and use of the taxi cost index. Key among these are:

- vehicle capital
- fuel costs
- hirings per car
- tyres, repairs and maintenance
- driver labour.

The Commission has developed an alternative pricing methodology that addresses these concerns as well as return on capital, ie plate values. The Commission invites comments on these issues, on the level of network costs, which are high relative to other states, and its assumption that bailee drivers generally receive 50 per cent of gross takings for each shift.

The new pricing model essentially sets out a profit and loss statement for the average taxi. From this, a surplus or deficit is derived. A surplus implies that fare levels should decrease. Conversely, a deficit implies that taxi operators require additional revenues to cover their costs and earn an adequate return, and therefore fares should increase.

If return on plate values is ignored, the Commission's new pricing model suggests a fare decrease is warranted. Including plate values suggests no price change should occur.

The new pricing model takes into account efficiency improvements. In its first review of taxi fares, the Commission raised concerns that the existing index did not share efficiency gains with consumers. With appropriate flexibility, application of the new pricing model will be able to reflect efficiency improvements.

3.2 Operating costs

The setting of taxi fares in the ACT has relied on the use of a 'taxi cost' index developed by the Taxi Industry Advisory Council, an advisory body to the ACT Government. Developed in 1989, the index has been used ever since as the basis for determining **changes** in taxi fares. The index is comprised of a number of cost items associated with the operation of a taxi. Rather than estimating the actual cost of providing a taxi in the ACT, it attempts to measure movement in operating costs over time.

From its inception, as the cost index was not designed to reflect taxi industry costs in an absolute sense, it was not used for setting absolute fare levels. Rather, it was designed to provide a reasonable basis to adjust fares to reflect cost escalation. ACT taxi fares have never been rigorously 'base-lined' against actual costs. When the taxi index was introduced, fares were adjusted on a 'reasonableness' basis, and have subsequently been adjusted using the model.

The existing taxi index contains all significant cost items involved in operating a taxi, and provides an annual cost estimate for each item for a typical operation (with typical annual kilometres, etc). The initial (1989) cost estimate for each item has been indexed annually using evidence of changes in actual costs (eg registration and third party insurance) or changes in 'standard' indices (eg CPI, average weekly earnings).

Attachment 3 sets out details of the cost index, including the basis of the cost estimate and Canberra Cabs estimate of costs at January 2001.

Canberra Cabs' submission to the Commission sets out in detail the costs for three scenarios:

- March 2000 – actual costs
- March 2000 – actual costs as adjusted by ICRC
- January 2001 – actual costs, as estimated by Canberra Cabs.

For the period March 2000 to January 2001, the submission shows the following increases in total costs:

- 5.70 per cent from actual March 2000 costs
- 7.81 per cent from the Commission's March 2000 costs (which were used as the basis for the previous (July 2000) fare increase).

On the basis of these costs and the current index, Canberra Cabs submits that the appropriate fare increase is 7.81 per cent.

3.2.1 Appraisal of existing taxi cost index

For the past decade, price increases in taxi fares have been based on estimated changes in the taxi cost index. This index sought to incorporate relevant cost components of taxi operations, but the absolute levels of those costs were not used to decide fare increases. Nor was any provision for productivity and efficiency changes incorporated in the model. Fare increases were based on relative movements in the total costs.

The taxi cost index has undergone little or no substantive change since its inception in 1989. In its previous price determination, the Commission expressed concern as to whether the index remained the most appropriate mechanism by which fare increases should be determined. Although historical emphasis has been placed on relative movements in the index, the Commission is of the view that a cost model which does not reasonably reflect absolute costs is unlikely to reasonably reflect changes in costs over time.

As part of a detailed review process, the Commission has assessed the current taxi cost index, with assistance of information contained in Canberra Cabs' submission (January 2001) and subsequent discussions with Canberra Cabs' representatives.

A detailed item-by-item appraisal of the current taxi cost index is presented in attachment 3.

The Commission has identified a number of major cost areas/issues that the current index model is significantly deficient in reflecting current typical taxi industry costs in the ACT:

1. vehicle capital (item 1)
 - current costs over-estimate average vehicle depreciation because they are based exclusively on the costs of new vehicles with a functional life of four years. They do not allow for the mix of new and second-hand vehicles in the fleet and the range of years for which each are used. A more reasonable working assumption would be to assume that 50 per cent of the fleet was new vehicles, which are sold after five years, and the remaining 50 per cent are on average three years old at purchase and are sold after a further four years
 - current costs are understated to the extent that they ignore any interest charges on vehicle capital (these are real financial costs, as most owners lease vehicles)
2. fuel (item 10)
 - costs are based on an average vehicle travelling 180,000 km per annum, whereas the current 'typical' estimate is 206,000 km per annum. A Canberra Cabs' survey figure gave an average of 190,400 km. However, Canberra Cabs advise that they do not place a high reliance on that survey figure, and that 206,000 km is a more accurate reflection of actual distance travelled
 - costs are based on LPG consumption of 5.0 kilometres per litre, whereas the current 'typical' estimate is 5.5 kilometres per litre. Canberra Cabs agree that this is a reasonable estimate
3. hirings per car
 - Canberra Cabs indicates in its submission (page 3) that average hirings per car in 2000 amounted to 11,708. This represents a 6 per cent reduction on the corresponding 1999 figure. The Commission has some concerns with this figure. Close analysis of demand figures for 1999 and 2000 indicate that the fall in demand in 2000 was concentrated in the second half of the year. Comparison of first half demand for 1999 and 2000 indicates that total demand grew by around 2 per cent, and telephone bookings by 3.3 per cent.

There is the strong likelihood that the fall in demand in the second half of 2000 was associated with reduced business activity during the Sydney Olympic Games. Discussions with Canberra Cabs indicate that the business market is a key driver of taxi demand in the ACT. This market reduced significantly in the

second half of 2000. The Commission considers it appropriate to adjust demand for the effect of the Olympics. A more reasonable annual estimate is assumed to be 12,145, which represents a 2.5 per cent reduction on the 1999 figure. Given the relatively high number of average kilometres adopted in the model (206,000), it has been assumed that the increase in average hirings has been accompanied by a corresponding reduction in dead kilometres.

4. tyres, repairs and maintenance (items 11, 12)
 - as with fuel, costs are based on 180,000 km per annum, whereas the current typical estimate is 206,000 km per annum
5. driver labour (item 14)
 - costs (including superannuation and workers compensation) are \$30,000 - \$35,000 per annum too high relative to actual earnings achieved by ACT taxi drivers
 - this item is the largest single contributor to the cost index, representing 55 per cent of total costs. Consequently, it has by far the greatest (absolute) divergence from actual earnings by taxi drivers, with the divergence accounting for 15 - 20 per cent of total costs.

Also, the current taxi cost index model does not include any allowance for the opportunity cost/interest charge relating to the cost of taxi plates.

In considering an alternative method for assessing future taxi fare changes, the Commission has sought not only to include adjustments to the more straightforward measures of costs, but also to reflect reasonable estimates of a more contentious element of a taxi cost index, ie driver labour costs, and to provide a mechanism for incorporating consideration of a return on taxi plates.

The Commission notes the industry's view that the cost index deliberately excluded any consideration of the return on plates and that the fares themselves are not designed to provide any investment return. The industry has indicated that the decision to enter and exit the industry is made independently of fare levels and is captured through changes in taxi plate prices. It is not clear to the Commission whether this position depends on the continuation of a regulated supply of taxis, which leads to higher prices for taxi plates, and would change if deregulation was introduced. However, even within a regulated environment, the prices of taxi plates can fluctuate, as evidenced in Canberra Cabs' submission (page 11).

In relation to driver labour, the current cost model links costs to a historical award for Commonwealth Government car drivers, subsequently adjusted according to annual changes in average weekly earnings. The Commission is of the view that such a basis does not provide an appropriate measure of labour costs for the taxi industry. On the one hand, the owner-driver will view the costs of his own labour as some measure of return after he has paid out-of-pocket expenses. On the other, the owner-driver will view the costs of bailee drivers as being the amount that he has agreed to pay the driver for the shifts worked. In most cases bailee drivers receive 50 per cent of the gross takings for those shifts. In neither case does the decision to own and operate a taxi or to work a shift for a taxi owner appear to be related to historical award rates for Commonwealth car drivers.

Another area where the Commission considers that the current cost model overstates typical costs is comprehensive insurance. The current index assumes that all vehicles are new. On the other hand, the Commission believes that there should be upward adjustments to workers compensation payments and illness/accident insurance premiums.

3.2.2 Development of new costing and pricing model

The Commission has constructed a costing and pricing model based on Canberra Cabs' submission, but with some modifications in cost items to better reflect typical cost levels, to encompass a more realistic treatment of labour costs, and to facilitate an assessment of the impact of a nominated return on taxi plates. The proposed model is similar to the model put forward by one of the NSW taxi companies in relation to IPART's review of the NSW taxi industry.⁴ Note that the IPART review did not review the fare setting methodology. The Commission has made some minor adjustments to the structure of that model, and modified it to incorporate operations and costs typical of the ACT taxi industry.

An additional cost item has been included in the proposed model to allow for administrative labour costs associated with running a taxi business. These were not included in the model submitted to IPART. This allowance covers approximately 3 hours/week by owner-drivers and 1 hour/week by bailee drivers, valued at the average driver earning rate. Whilst these figures are not based on any survey evidence, they appear plausible for the administrative tasks involved. This adjustment increases the cost base.

The Commission is concerned with the level of the network fee at \$11,854 per vehicle. Representing the average costs of operating and maintaining the Canberra City operation including, in particular, the radio dispatch network, this figure is taken from Canberra Cabs' data. Initial examination of interstate data indicates that this figure is relatively high compared to interstate costs. For example, the IPART report notes that network fees in NSW are around \$5,850.⁵ Further, the ACT Government has recently called for tenders to offer an additional network service. It may reasonably be expected that competition at the network level will lead to reductions in ACT network fees. Given these observations, the Commission is concerned to incorporate an appropriate level of network fees in the fare setting methodology, which may be lower than those currently stated. The Commission invites responses about the level of network fees applied in Canberra.

The new model essentially provides a profit and loss statement for a typical taxi operation in the ACT from the perspective of the vehicle owner. It relates to a single vehicle operating for 206,000 km (7,150 driver hours) per year. Two sub-models have been developed: one assuming the owner drives (55 hours/week) and also sub-contracts to bailee drivers (88 hours/week), and the other assuming 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. Clearly, changes to this proportion can have significant impact on total costs. The Commission invites comments from the industry as to whether this proportion is reasonable.

A summary of model results based on current fares and January 2001 expenses is given in the table below. A detailed derivation of each cost item is provided in attachment 4. The pricing implications of using this model are discussed in chapter 4.

⁴ IPART, *Review of the taxi cab and hire care industries*, Final report, November 1999, p 62.

⁵ IPART, *Review of the taxi cab and hire care industries*, Final report, November 1999, p 60.

A revenue figure is first derived for the average taxi. The gross takings figure is based on 12,145 hirings per car and an average fare per hire of \$13.964. This fare is based on the average distance per hire of 8.8 km and existing fares. Non fare income is Canberra Cabs' estimate of trading and investment rebates available to Canberra Cabs members.

Table 3.1 Proposed ACT taxi pricing model

	Annual cost – January 2001	
	Owner-driver + bailee drivers	Bailee drivers only
REVENUES		
Gross takings	169,595	169,595
Non-fare income	3,895	3,895
Total Revenue	173,490	173,490
OPERATING EXPENSES		
Fixed Costs		
Vehicle capital costs	5,354	5,354
Vehicle registration costs	6,757	6,757
Driver licence & medical	61	-
Safety camera	600	600
Comprehensive insurance	4,410	4,410
Network fees	11,854	11,854
Office/miscellaneous expenses	2,205	2,205
Sub total	31,241	31,180
Variable Costs: Non-labour		
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	39,949	39,949
Variable Costs: Driver labour		
Driver payments (bailee drivers)	52,183	84,797
Administration labour (bailee drivers)	1,225	1,838
Workers compensation insurance (bailee drivers)	1,884	3,027
Illness/accident insurance (owner driver)	2,028	-
Sub total	57,320	89,662
Total Operating Expenses	128,510	160,791
Gross Surplus (Rev-Op Exp)	44,980	12,699
Return on owner-driver labour ¹	34,391	-
Surplus after return on labour, ie net surplus	10,589	12,699

1. Based on 58 hours/week, (including 3 hours' administration) 50 weeks pa, \$22.865/2 per hour (ie same rate as earned by bailee drivers).

Cost estimates are then derived for the average taxi. This is largely based on information provided by Canberra Cabs, although adjustments have been made to a number of cost items as outlined in section 3.2.1. Taking total revenue and total operating expenses, for each sub-model, a gross surplus to the owner is derived before any return on his/her labour or the value of taxi plates. Consideration can then be given to reasonable returns on these items and the effects of these assumptions on the 'net' surplus.⁶

After allowing for a reasonable return on owner-driver labour (equal to the hourly rate earned by bailee drivers), the owner surplus is about \$10,600 - \$12,700 per annum. This represents a 6 - 7 per cent margin on total revenues.

Ignoring the opportunity cost of plates, this indicates that a zero surplus could be obtained if fare revenues were reduced by \$21,200 - \$25,400 per annum (around 12 - 14 per cent), ie twice the owner surplus figure. This assumes that the fall in revenue is brought about through a fall in the average fare level only and that costs/distance travelled remain unchanged. Further, it is assumed that bailee driver payments are reduced pro rata.

The above suggests that if the return on plate values is ignored, taxi fares in the ACT are currently over recovering costs. The Commission believes that if a return on plate values is included in the cost index, no fare change is warranted. Issues relating to plate values are considered in the following chapter.

3.3 Efficiency

The current taxi cost index model is based on the historical costs of a pre-determined set of inputs, adjusted periodically by standard indices (eg CPI, average weekly earnings, price of fuel). It thus cannot allow for changes in efficiency in the use of inputs (eg fuel consumption) or changes in productivity (eg extent of dead running relative to revenue running).

On the other hand, increases in costs involved to achieve efficiency/productivity gains may be included in the model (eg higher vehicle capital costs, increased network fees relating to the computer dispatch system).

This uneven treatment of the cost changes associated with efficiency/productivity improvements is clearly a deficiency in the current taxi cost index model and is one reason the model should be reviewed and re-based periodically.

The proposed costing and pricing model will largely overcome the above deficiencies, if applied with flexibility. The model is designed to reflect the absolute costs and revenues of a typical taxi operation. All inputs should be reviewed on a periodic basis, including the assessment of the impact on costs and revenues of any changes in efficiency/productivity, eg:

- any significant change in fuel consumption rates should be incorporated into the fuel cost component
- any significant change in hirings (or hiring kilometres) per taxi per annum should be incorporated into the revenue component

⁶ Additional details on the calculation of profit and loss figures presented in the table 3.1 are given in attachment 4.

- any significant change in typical total taxi kilometres per annum should be incorporated into the variable cost components.

In this way the proposed model should continue to reflect the absolute costs and revenues for a typical Canberra taxi operation, including any changes in efficiency/productivity.

In practice, efficiency/productivity changes are likely to occur only slowly (eg fuel consumption), and therefore a simplified price indexation approach for such items may suffice in the short/medium term, with a more detailed review (say) every 5 years.

Service quality issues and efficiency issues overlap with fare setting. The Commission notes that the Memorandum of Understanding (MoU) between the ACT Government and Canberra Cabs refers to minimum service levels in terms of maximum waiting times. Other measures could be used to ascertain industry performance. These could assist in determining the basis for price setting. Such key performance indicators are designed to benchmark performance relative to interstate taxi operations to assist in assessing deficiencies. They may also impact indirectly on fare setting decisions. Such measures could include:

- fares
 - fare v distance (day/night)
 - fare for average trip
- fleet size
 - total fleet numbers (taxis/000 population)
- key operations and revenue statistics
 - total kilometres per annum/taxi
 - revenue kilometres per annum/taxi
 - total hirings per annum/taxi
 - total earnings per annum/taxi
 - total driver hours per annum/taxi
- service quality indicators
 - taxi waiting times:
 - phone bookings v rank waiting
 - weekday afternoons v other periods
 - airport v other locations
 - WATS v standard vehicles.
 - telephone answer waiting times (and missed calls)
 - customer satisfaction surveys
 - complaints (with breakdown by type).

The Commission notes that much of this information is already collected through the MoU and the ACT Government industry survey (see chapter 5 on service quality).

The current taxi cost index model does not translate efficiency gains from the above factors into lower fares. Efficiency gains would accrue to owners/drivers through higher earnings (greater productivity per operating hour) or a higher profit/rate of return.

Unless an explicit decision was taken to increase the labour cost rate or the rate of return on plates, the proposed costing/pricing model should effectively translate most cost efficiency gains into lower fares for consumers. However, revenue efficiency gains (eg takings/driver hour) would translate 50 per cent into gains to drivers (as their hourly rate is equal to 50 per cent of the takings), 50 per cent in gains to consumers (as the change in 'bottom line' profitability in the model would translate to lower fares).

As noted earlier, the pricing system will provide substantial incentives to owners/drivers to improve efficiency. The key issue is the trade-off between 'service quality' and 'efficiency' aspects. The major impact on achieving greater efficiency through lower costs is by reducing the amount of dead (ie non revenue-earning) kilometres. In terms of service levels, there may be a trade-off for taxis between fast response times and seeking to minimise dead kilometres, particularly in a dispersed, low-density environment such as the ACT. The Commission notes Canberra Cabs' view that the data dispatch system results in better response times but perhaps more dead kilometres. On the other hand, Canberra Cabs suggests that the appropriate use of GPS should enable waiting times to be reduced and probably also dead running kilometres.

In an environment where there is a limited supply of taxis and where there is no fare differentiation, the Commission welcomes responses on how a fare structure could better reflect different levels of service.

4 PRICING AND CONSUMER PROTECTION

Under section 20 of the *Independent Pricing and Regulatory Commission Act 1997*, the Commission is to consider a range of factors relating to pricing and consumer protection:

- 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 – section 20(2)(a)
- the social impacts of the decision – section 20(2)(g)
- the effect on general price inflation over the medium term – section 20(2)(j).

Factors relating to price are addressed in this chapter. Service quality issues are considered in chapter 5.

4.1 Conclusions

The Commission has identified problems inherent in the existing taxi cost index. In particular, the cost index is not a reasonable reflection of typical industry costs or changes in costs. In light of this, the Commission has developed an alternative cost and pricing model. However, some issues in regard to pricing have still to be resolved. In terms of costs, a key issue is the inclusion of a term accounting for a return on plate values.

Key issues in regard to plate values are:

- whether a return should be reflected in fares – the Commission notes the industries position that fares were never intended to provide a return on the investment in the taxi licence/plate
- what should the value of plates be – buyers of plates would have purchased their taxi licences at different times, hence paying different amounts
- what is a reasonable return on the value of plates.

The Commission invites comments on these issues.

The Commission's analysis suggests a return of taxi plate capital of 4.2 per cent given current fare levels and plate values of \$280,000. On average, the purchase price of plates is expected to be lower than this figure, and the return consequently higher.

If a return on plate values is included in the determination of fares, the Commission considers no change to current fare levels is warranted.

Recommendation 1 – Maximum fares

The Commission recommends that there be no change to the level of maximum taxi fares from 1 July 2001 – 30 June 2002.

Apart from the issue of costs to be included in fare levels, the Commission has considered the structure of fares. Relevant issues include:

- flagfall v distance rate: what is the appropriate balance between the flagfall and distance components of the fare, should there be varying flagfall rates depending on time of day?
- multiple hiring and maxi cab rates: what is the appropriate relationship between the standard taxi rate and multiple hire and maxi cab rates?
- peak and off peak rates: existing rates in the ACT differentiate between 'daytime' operations and night time operations (9pm - 6am everyday). Whilst this recognises high demand during Friday and Saturday nights, the Canberra market also exhibits some peak demand during weekday mornings and late afternoons
- standard taxis and WATs: taxi fares are the same for both taxi types. However, WATs are likely to have higher operational and capital costs associated with the vehicle. Countering the suggestion that this should lead to different fares is the observation that WAT licences are inexpensive compared to standard taxi licences.

In some cases the Commission considers differential pricing may achieve little in terms of encouraging supply, as taxis are on the road for the majority of each day. Whether differential pricing influences demand will depend on the nature of demand. The Commission invites comments on whether a more disaggregated fare structure is warranted.

Recommendation 2 – Fare structure

The Commission recommends that the existing fare structure be maintained, with a review to take place when maximum fares are again considered by the Commission.

4.2 Pricing

In its previous price determination, the Commission permitted a 7.71 per cent increase in average taxi charges based on cost increases derived from the current taxi cost index model. In addition, a further 7.85 per cent GST adjustment was incorporated after allowing for cost savings from the Federal Government's ANTS (A New Tax System) package. However, the Commission stated at that time that it did not intend to use that taxi cost index for price setting from July 2001.

The protection of consumers from abuse of monopoly power through prices can be achieved most appropriately through a proper determination of costs. Issues surrounding cost items to be included in the determination of fares have been discussed in the previous chapter. The Commission is satisfied that the cost items and their values are appropriate for fare setting purposes, and that they protect consumers from any abuse of monopoly power. However, some issues do remain in regard to cost items, particularly in relation to the inclusion of a return on plate values item. These issues are further discussed below.

The Commission has identified major weaknesses in the current taxi cost index approach to fare setting:

- the cost index is not a reasonable reflection of typical industry costs or changes in costs
- the prices have never been 'base-lined' as to their appropriateness: when the current taxi cost index was introduced, it was assumed that the initial price levels were appropriate, and indexation started from there
- the cost index does not reflect any changes in industry productivity or efficiency
- previous price determinations have been based on annual movements in the current taxi cost index, irrespective of the accuracy of individual components.

The Commission has reviewed the current model and developed an alternative model with a substantially different structure. It is not possible to undertake a direct comparison of the results of the two approaches. The Commission considers that it is appropriate to use the proposed model to make price decisions based on the intrinsic merits of the components.

4.2.1 Plate values/return on capital

On the basis of the data in table 3.1, the surplus available (average gross revenues less fixed and variable costs) after adjustments for return on owner-driver labour is between \$10,600 and \$12,700. This represents a 6 – 7 per cent margin on total revenues. In a conventional profit and loss statement, this surplus would be assumed to cover the return on capital – in this case, the return on the value of the taxi plates. The Commission notes Canberra Cabs' view that the fares and the previous cost index have not explicitly incorporated a return on capital and that the purchase of taxi plates is driven by a number of considerations. The Commission infers that the purchase of a taxi plate is made in the expectation that the purchaser is buying an asset with a future net income stream; an asset which, on the basis of restricted supply, will provide the likely opportunity for increased capital value. A purchaser is not compelled to buy a plate. Presumably he/she has the opportunity to acquire alternative investments, and would do so if he/she believed the net return would be greater than the acquisition of a taxi plate.

In adopting an industry model for price setting, the Commission is aware of the difficulty in representing the 'average' taxi. Obviously, there are taxis on both sides of this average. However, if it is appropriate to apply a figure for average gross revenues and a figure for average fixed and variable costs, there is a case for assuming that the derived surplus represents an average return on the value of the plates. In determining a mechanism for establishing a medium term price path, the Commission aims to apply a reasonable measure of a return on capital which can be applied over time. Therefore, the Commission believes it is appropriate to apply a cost index model which takes into account the implicit annual return on the investment in plates.

Two major issues must be considered in relation to plate values: the historical values of plates and future changes in plate values. The following analysis is based on recent historical data. The following table provides some measures of taxi plate values over time.

The real cost data in the table below was sourced from the Australian Taxi Industry Association (1999) and adjusted according to CPI changes. The sale price and auction price data were sourced from the Canberra Taxi Proprietors Association and Aerial Taxi Cabs' submission to the Freehills review.

Table 4.1 Values of ACT taxi licences

	Real cost of ACT taxi licences	Sale price of ACT taxi licences	Auction price of ACT taxi licences
1991	\$234,643	na	na
1992	\$260,688	na	na
1993	\$317,274	na	na
1994	\$311,374	\$280,000	\$241,000
1995	\$250,587	\$240,000	\$162,000
1996	na	\$240,000	no auction
1997	\$243,597	\$250,000	no auction
1998	\$280,000	\$260,000	no auction
1999	na	\$280,000	no auction

Source: Freehills Regulatory Group, *National competition policy review of ACT taxi and hire car legislation*, Final Report, March 2000, pp 39 and 131.

The data indicates that there has been a strong and consistent market for taxi plates in the ACT during the 1990s. Prices in the secondary market significantly exceeded auction values in those few years when auctions were held. However, many plate owners would have acquired their plates a long time ago and could be expected to have received an adequate return on their investment over that time. If that had not been the case, it is unlikely that the current prices of plates would be as high as they are.

The calculations of the surplus in table 3.1 imply an average return on taxi plate capital of 4.2 per cent under current fares and on the basis of a current plate value of \$280,000. Of course, not all current owners of plates paid that amount for their plates.

The Commission does not have any evidence as to the average length of time that a taxi plate licence is held, particularly as they are traded in a secondary market. Given the above data, it is reasonable to assume that the implied returns to capital, based on a range of historical prices, are higher than 4.2 per cent. A purchaser of a taxi plate at auction in 1995 could expect, under the proposed model, to enjoy a return of 7.2 per cent on the historical value of the plate, and that does not include the capital gain which he/she would enjoy if the plate was sold at current market prices.

When we consider the capital gain potentially made by some licence owners, the return could be in excess of the 7.2 per cent figure above. Based on a taxi plate price of \$162,000 in 1995 and assuming values of \$280,000 in 2001, the annual average increase in the capital values of the taxi plates over this period is over 9.5 per cent per annum. The combined return that some licence owners appear to be receiving is relatively high when we consider returns from other investment options.

The analysis above suggests an annual return of between 4 – 7 per cent, with the rate tending to be at the lower end of the range, based on higher plate values recorded over the 1990s. This excludes the significant capital gains that some licence owners would have made and could expect to make if they sold their plates at current prices.

Given that plate owners can dispose of those plates at any time and the value of those plates reflects current values, the Commission believes that a return closer to 4 per cent on current

plate values is appropriate. The Commission considers it reasonable to apply a rate of return of 4.2 per cent on current plate values. As the model implies, this supports the outcome of no fare increase.

It should be noted that the return of 4.2 per cent on current plate values of \$280,000 represents a higher return for those who purchased plates at much lower historical values. Further, the current position of Canberra Cabs is for plate values not to be reflected in the fare setting methodology. Such an approach would suggest a significant fall in fares, and is indicative of an over recovery of costs through fares given no allowance for a return on plate values.

The Commission has also considered how plate values should be treated in the price setting methodology going forward. It is important that the treatment of capital be consistent with any potential changes to the structure of the industry and that pricing outcomes be reasonable. If there was a significant increase in the number of taxis either through a sale of additional plates or through deregulation, there would be a general expectation that the value of each plate would fall. Allowing this to flow through the new pricing model calls for lower fares or at least lower increases in fares.

Conversely, if the value of plates increased significantly, the relative reduction in supply, commensurate with the demand reflected in higher plate values, would be consistent with the requirement for higher fares. These outcomes could lead to undesirable volatility in the level of fares. The Commission believes that it is appropriate to set a fixed plate value in the fare setting process to avoid some of this volatility. Further, the Commission notes volatility in calculated fares can also be associated with the rate of return. The Commission considers it appropriate that the absolute dollar return on plates should be fixed for the medium term.

Thus in moving forward, it is the Commission's intention to consider a fixed plate value in the price setting methodology, as well as a fixed percentage return. The Commission will apply a return of 4.2 per cent on a plate value of \$280,000 when calculating the future deficit/surplus from the new pricing model. These factors plus other cost items could be rebased every five years or so. In the interim, annual percentage changes and efficiency and operational changes can be considered in the fare model, given a fixed dollar return for plate values.

4.2.2 Fare structure

The Commission notes that the new model focuses on establishing a required revenue outcome. It does not address the issue of fare structure. The model provides no way of determining any differences between a flagfall and per kilometre charge, nor whether there should even be a distinction. The Commission is of the view that the principal objective of a fare structure is to ensure that the correct signals are sent to consumers and producers, reflecting the value and the cost of the services being provided.

In its last price determination, the Commission made adjustments uniformly across all components of the fare structure, covering both flagfall and per kilometre charges for the different rates (ie rates 1 – 6). In its submission to this current review, Canberra Cabs offers two alternatives to applying its suggested 7.81 per cent increase. This could be applied as before, uniformly across categories, or alternatively, it suggests that the flagfall components remain unchanged and the per kilometre charges be increased to produce a net increase commensurate with their overall recommendation.

Flagfall v distance rate

While the Commission is of the view that no fare increase is warranted, it has nonetheless considered the structure of fares. Canberra Cabs has expressed the view that there may be consumer opposition to a higher flagfall relative to the per kilometre charge. On the basis of an average trip of 8.8 kilometres under the current fare structure, the flagfall represents between 20 per cent and 25 per cent of the total fare, depending on the rate applied.

The Commission notes that previous price directions were calculated on the basis of an average trip of 8.8 kilometres. The Commission has been advised that over time the average taxi trip distance has increased as Canberra has grown. This has contributed in large part to increased dead kilometres. To the extent that this trend continues, the Commission notes that a shift in the fare structure towards a higher per kilometre charge relative to a flagfall will lead to higher weighted fares. However, the Commission considers that any modest re-alignment of the flagfall and distance charge for an average trip is not likely to lead to any material difference in effective fares.

The current fare structure acknowledges a differential between day rates (1, 3 and 5) and night rates (2, 4 and 6) rates, with the latter higher presumably to provide an incentive to have taxis available when the demand is generally lower. The night rate is about 15 per cent higher than the day rate. These differentials are reflected solely through the per kilometre charges. Flagfall rates remain the same, irrespective of time of day.

The Commission notes that there are significant interstate variations. These are illustrated in the table below and show that there is no consistent pattern.

In terms of producing appropriate price signals to the market and reflecting legitimate differences in cost structure, the Commission considers there is little justification for per kilometre charge differences. This is because the variable costs of operation are generally the same, irrespective of the time of the day. In theory, there may be a case to provide a differential flagfall to provide an incentive to offer services.

Table 4.2 ‘Night’ standard cab rates compared with ‘day’ rates

State	Flagfall	Distance	Night hours
NSW	same	+20%	10pm-6am everyday
Victoria	+39%	same	midnight-6am everyday
Queensland	+48%	same	8pm-6am Mon-Fri; 1pm Sat-6am Mon
South Australia	+91%	+7%	7pm-6am Mon-Fri; Sat and Sun
Western Australia	+45%	same	6pm-6am Mon-Fri; Sat and Sun
Tasmania	same	+20%	8pm-6am Mon-Fri; Sat and Sun
ACT	same	+15%	9pm-6am everyday

Source: Various taxi councils.

The Commission notes that during weekday and weekend night time periods in the ACT, most taxis are connected to the network, ie on the road. This suggests that additional incentive to operate during these times is not required. This proposition is supported by the observation that on weekend (Saturday) nights, the proportion of taxis engaged is very high, reaching 95 per cent at times. The current market environment suggests that most taxis are

on the road in the evenings, and are often engaged. This does not support a flagfall differential, but may be used to support additional taxi licences to meet demand.

Nonetheless, the Commission is interested in receiving submissions on whether a fare differential by time of day is appropriate, and if so, how the differential should be applied to the flagfall or distance components.

Multiple hiring and maxi cab rates

There are different rates for multiple hiring (rates 3 and 4) and for maxi cab hirings (rates 5 and 6). The Commission has had little information supplied to it about the frequency of multiple hirings and the frequency of maxi cab hirings. The historical convention of having different rates for these services and the differences being 75 and 150 per cent respectively has not been revisited in detail. As a consequence, the Commission invites comments on whether there are more appropriate methods of differentiating these services from the standard cab fare.

Peak and off peak rates

Despite the varying fare rates, the structure does not distinguish between peak and off peak demand, eg morning and afternoon weekday peak periods. In principle, to facilitate a better balance between supply and demand, there would be grounds for considering fare differentials to encourage better waiting time performance at peak times. In chapter 5, the Commission considers Canberra Cabs' performance. The information available suggests that overall, current peak period waiting time requirements for standard taxis are easily achieved. The current performance requirements define the peak period as 3 - 6pm, Monday to Friday. Outside these times, the 85 per cent target is only just achieved. Whether this suggests a need for differential peak and off peak prices is unclear. A review of performance requirements may be more appropriate.

By definition, peak times are when the demand is greatest, and it may be expected, willingness to pay is also greatest. However, on the basis of the current supply conditions, evidence proffered by Canberra Cabs suggests that the majority of taxis are already available throughout the morning and afternoon peaks. Consequently, under current conditions, any am and pm peak pricing differentials would be unlikely to increase the supply of taxis, and waiting times would remain substantially unchanged. Nonetheless, the Commission invites comments on the desirability of more price variations by time of day.

Standard taxis v WATs

The other major fare issue refers to the difference between standard taxis and WATs. Currently, fares are identical for both types of vehicle, even though vehicle costs for the latter are higher. Neither the existing cost index model nor the proposed cost and pricing model have been constructed to incorporate WATs. Whilst the existing model deals with annual changes only, the proposed model can be applied to measure costs for WATs separately from standard taxis.

In general terms, assuming an identical average gross revenue, operating costs for WATs may be expected to be higher as the vehicles are more expensive and are likely to incur higher fuel and maintenance costs and higher fees to access the current cab dispatch network. Offsetting these higher costs is the low licence fee of \$1,000 annually. WAT

licences are issued for six years, are not transferable and are surrendered at the end of the period to the Department of Urban Services. No plate values attach to these licences.

Although the Department of Health issues taxi vouchers for disabled passengers, the fares earned by cab drivers are the same for all passenger, despite the additional costs associated with loading/unloading disabled passengers. The Commission understands there may be limitations in introducing differential fares as they may be viewed as discriminatory. However, there may be reasons for having additional fixed charges associated with the extra time required to serve disabled passengers using WATs. The Commission is interested in obtaining views on whether there is a case for WAT cab drivers to earn higher fare revenue for disabled passengers, and if so, what the payment mechanism should be.

The Commission considers that the market environment in the ACT suggests the existing fare structure be maintained. The Commission's proposal that there be no change to existing fare levels also suggests that the fare structure should not be altered. Nonetheless, the Commission invites comments on whether to vary the existing fare structure.

4.3 Social impacts

The Commission's first determination resulted in taxi fares increasing by around 14 per cent. This was due to a combination of cost increases and the introduction of the goods and services tax. At that time, the Commission considered closely the social impacts of fare increases.

The Commission is aware of the importance of taxi transport to particular community groups. In particular, some people with disabilities are reliant on taxi travel as buses are not a viable alternative. The Commission's preliminary analysis in this draft report suggests that no fare increase is warranted. Obviously, there are no concerns in regard to the inflationary effects on individuals and inflation in the ACT arising from this proposal.

The Commission also notes that the ACT Government runs a taxi subsidy scheme which is designed to assist people with permanent or temporary disabilities who need to use taxis.

4.4 Price path

The Commission stated at the time of the previous price direction that it was looking to establish a process which would allow it to provide for price directions of longer than one year. This was desirable to encourage efficiency improvements in a regulated industry where the benefits could be shared between consumers and producers.

As an effective profit and loss statement, the proposed pricing model takes into account revenues and costs. It facilitates assessment of an appropriate annual rate of return on the capital values of taxi plates. As outstanding decisions on the structure of the industry have yet to be made by the ACT Government, the Commission is aware of the need to ensure that its price direction will not prove inconsistent with any such decision. In particular, any changes which may lead to increased competition, could be expected to lead to lower costs for the same level of demand, and thus a reduced requirement for fare increases, or even reductions in fares.

The Commission has not applied the new pricing model to set fares for a two year period, despite it considering that recurrent annual price directions alone will produce little in the way of efficiency improvements. Exogenous changes to the industry can be expected to have a significant impact on the structure and operation of the industry. In the light of this expectation, the Commission considers it is more appropriate to provide only a one year determination, based on the new pricing model. At the same time, it will monitor the effects of changes over the next 12 months and be in a better position to issue a medium term direction from 1 July 2002.

4.5 Proposed maximum fares

Canberra Cabs' submission recommends an overall fare increase of 7.81 per cent. Assuming that is translated straight through to the gross revenue line with no other increases in costs, the surplus after return on labour would amount to an additional \$13,550, ie between \$24,150 and \$26,250. Taking the midpoint produces an implied annual return on current plate values of 9 per cent, which exceeds the top end of the range (7.2 per cent) based on the lowest taxi plate price (\$162,000) recorded in table 4.1.

In the light of the above analysis, the Commission considers that the proposal to increase fares by 7.81 per cent, as advocated by Canberra Cabs, is not justified. The Commission notes that if a return of 4.2 per cent on current plate values is accepted, there will be no case for an average increase in fares on the basis of the proposed pricing model.⁷

The return of 4.2 per cent on a plate value of \$280,000 effectively represents a higher return for those who purchased plates at much lower historical values. Further, the current position of Canberra Cabs is that plate values not be reflected in the fare setting methodology. Such an approach would suggest a significant fall in fares, and is indicative of an over recovery of costs through fares given no allowance for a return on plate values. Given these factors, the Commission prefers to include plate values in the fare setting methodology, applying a 4.2 per cent return. The Commission is satisfied that overall this proposal for no change in fares is reasonable and justified.

⁷ It should be noted that the Commission's new cost and pricing model is based on existing fare and cost levels. The Commission has taken into account cost increases that Canberra Cabs have identified. The new cost and pricing model explicitly accounts for the current costs of providing a taxi service in the ACT.

5 SERVICE QUALITY

5.1 Conclusions and recommendations

The MoU sets out aspects of the relationship between the ACT Government and Canberra Cabs, the operator of the radio taxi network in the ACT. In particular, the MoU establishes performance requirements that Canberra Cabs must meet.

The Commission has reviewed the nature of taxi demand in the ACT and aspects of service quality supplied by Canberra Cabs. Taxi demand exhibits clear peaks and troughs on both a yearly, weekly and daily basis. The supply of taxi services must be sufficient and flexible enough to meet these varying patterns of demand.

The proportion of taxis engaged between 5:00am and 7:00pm on weekdays is often over 80 per cent. For weekends, the proportion of taxis engaged is over 60 per cent for around 20 hours each day. During high demand periods, engaged rates reach around 95 per cent on both weekdays and weekends. These figures are very high compared to Sydney taxis, and support the notion that an increased number of taxis may be warranted in the ACT market. In low demand periods the proportion of taxis engaged falls from these high levels, as in other cities.

Factors such as demand and proportion of taxis engaged influences waiting times. Canberra Cabs is required to achieve waiting time targets set by the MoU. For standard taxis, peak period targets are easily achieved. Interestingly, the 85 per cent of customers experiencing a waiting time of no more than 10 minutes target during off peak periods is only just achieved.

The Commission considers that waiting time targets for standard taxis during peak periods should be reviewed. Currently, the 85 per cent target allows for additional waiting time of 80 per cent (from 10 minutes to 18 minutes) when moving from 'all other times' to peak period times. It may be that since the peak period waiting time target is achieved easily, it may not be contributing to on going improvements in service quality. It is being met by default.

The existing targets may not properly reflect actual peak periods for taxi demand. The narrow achievement of some standard taxi waiting time targets suggests this is the case. However, as discussed above, it may be appropriate to actually tighten the existing 'peak period' target, moving towards convergence of the peak and off peak waiting time targets.

The Commission notes that demand 'hot spots' can occur on a random basis, as opposed to the general peak period that is expressed in the maximum waiting time service requirements. In this regard, the network operator is trialing new processes to identify and target these hot spots, thereby maintaining/improving its level of service provision.

Canberra Cabs generally does not meet its waiting time requirements in regard to WATs. The Commission is particularly concerned at this outcome given disabled users of this service often have limited alternatives. The ACT Government's issuing of an additional 10 WAT licences and more stringent enforcement of licence requirements is supported in this regard. The Commission understands that the ACT Government is also considering

incentives for WAT operators, eg specific charges that reflect the additional costs of providing a WAT service.

The Commission also notes that Canberra Cabs will be required to manage WATs to promote improved service levels to disabled users of such services. A previous management process existed up until around 12 months ago. The removal of this system does appear to have contributed to reduced service levels for WAT customers.

The recent survey of taxi industry performance is consistent with the above conclusions for standard taxis and WATs. Waiting times have deteriorated over the past year, and required performance targets have often not been achieved.

The survey indicates that customers are generally very satisfied with the service standards of Canberra Cabs. It is often argued that service standards would fall in a deregulated environment. The Commission does not necessarily agree with this position. In a deregulated environment (ie where quota restrictions are removed), the government can still set minimum service standard requirements, and continue to monitor service standards. The government maintains the right to license/authorise networks, operators and drivers, and impose appropriate sanctions if service standards are not met. Further, deregulation and competition have the potential to provide a more appropriate mix of service quality (where still meeting minimum requirements) and price options.

Recommendation 3 – Service quality

The Commission recommends that:

- service quality indicators in the MoU be reviewed, with particular attention paid to tightening peak period waiting time requirements
- improved monitoring of WAT service standards be implemented, with appropriate sanctions imposed where licence conditions are not met. Government and industry must work together to improve WAT service standards
- administrative actions required of Canberra Cabs by the MoU, eg independent audit of quarterly reports, be properly enforced and/or reviewed.

5.2 Introduction

The primary justification for regulating the taxi industry is that in an unregulated environment quality standards will suffer, with the cost of such a deterioration borne by rank and hail customers who have little ability to pick and choose between taxis.

In regulating the taxi industry, a trade off must be made between price, quality and waiting times, all of which relate to the service received by the customer. Taxi fares are now formally regulated by the Commission. Other aspects of service quality are covered within a Memorandum of Understanding between the industry and the ACT Government. The ACT Government also conducts an annual survey on taxi service quality.

Under section 20 of the *Independent Pricing and Regulatory Commission Act 1997*, the Commission is to consider a range of factors relating to service quality:

- 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 – section 20(2)(a)
- standards of quality, reliability and safety of the regulated services – section 20(2)(b).

These factors are addressed in the following sections.

5.3 Memorandum of understanding

On 20 June 1997, a Memorandum of Understanding (MoU) was signed between the ACT Government and Aerial Taxi Cabs Co-operative Limited (ie Canberra Cabs, operator of the taxi network in the ACT). The MoU is to operate from 1 July 1997 to 30 June 2002, and covers the services to be provided by Canberra Cabs in respect of a taxi booking service.

Schedule 3 of the MoU sets out performance measures and reporting requirements that Canberra Cabs must meet. Quarterly reports are required from Canberra Cabs covering the following performance measures:

Maximum waiting times

A taxi service must be provided so that:

On Monday to Friday afternoon between 3pm and 6pm the following standards are met:

- 85 per cent of hirers experience a maximum waiting time of no more than 18 minutes
- 95 per cent of hirers experience a maximum waiting time of no more than 30 minutes.

At all other times the following standards must be met:

- 85 per cent of hirers experience a maximum waiting time of no more than 10 minutes
- 95 per cent of hirers experience a maximum waiting time of no more than 20 minutes.

These standards apply separately to both standard and wheelchair accessible taxis (WATs). They are minimum service levels required of Canberra Cabs under the MoU.

Further, in no zone within Canberra Cabs' network should more than 40 per cent of hirers experience a waiting time of more than 10 minutes.

Response times

Canberra Cabs is also required to provide information separately for standard and WATs on response times for hirers requesting taxis by phone. Response times are classified into:

- less than 5 minutes
- between 5 minutes and 10 minutes
- between 10 minutes and 15 minutes
- between 15 minutes and 20 minutes
- between 20 minutes and 30 minutes
- between 30 minutes and 60 minutes

- more than 60 minutes.

Details of Canberra Cabs' performance in relation to the above requirements, and additional service quality information, is presented below in sections 5.4 and 5.5.

Other matters

Service quality covers issues broader than just waiting times. Issues such as driver knowledge and ability, and vehicle cleanliness and condition are also important. Such matters are covered within the MoU, which requires Canberra Cabs to take all reasonable steps to have in place procedures to ensure that:

- all taxis are clean and tidy when performing the service
- the interior of all taxis are maintained as smoke free zones
- all taxis have fully functioning air conditioning from 1 December 1999.

Canberra Cabs itself has conducted quarterly vehicle inspections since 1992. The entire fleet is inspected on a single day. The inspection concentrates on vehicle and driver presentation. Vehicles not meeting the required standards are given on the spot written notices of the defect, with a time/date by which the defect must be repaired. Any defect associated with safety requires an immediate response. Operators may be given two weeks to have minor defects corrected. Vehicles that do not comply are suspended from the radio network.

These service quality issues are further discussed in section 5.5.

5.3.1 Fines and sanctions

In instances where Canberra Cabs is found to have breached the MoU requirements, fines may be imposed. Fines have been imposed in the past, but have not been material in magnitude. The ACT Government may also suspend or withdraw any taxi network contract, operator accreditation or driver authorisation in the ACT. Such sanctions have not been applied to date. Failure to comply with the MoU is reason for terminating the contract between the ACT Government and Canberra Cabs for the provision of a radio network service. In such circumstances, Canberra Cabs would be given at least 20 business days to rectify the problem.

5.4 Passenger demand and waiting times

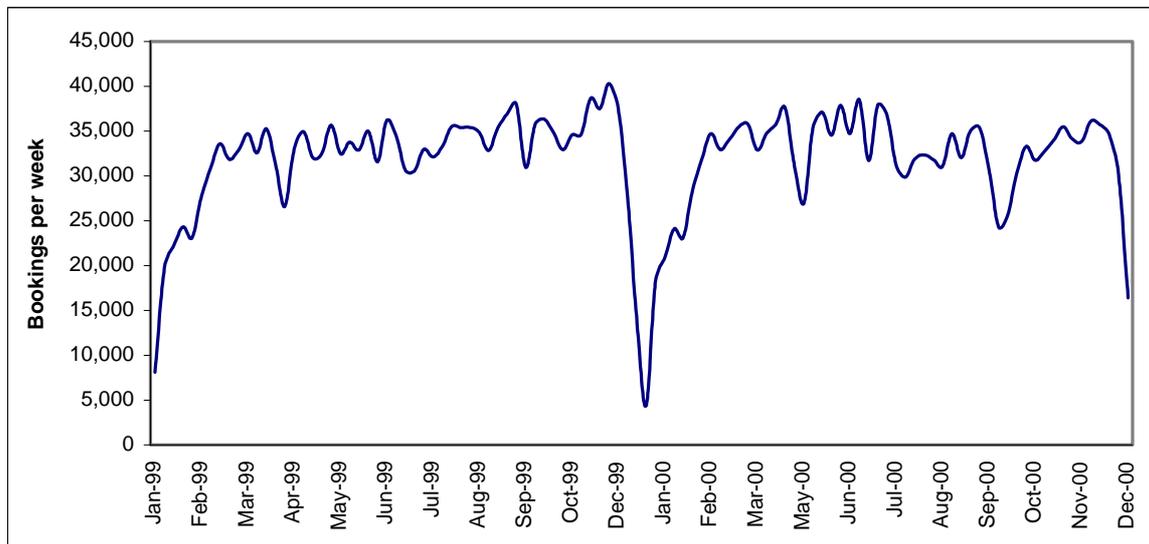
In this section passenger demand for taxis is considered in terms of variations over a day, week and a year, ie a short term view, and also in terms of demand trends over recent years.

5.4.1 Variations in demand

Information on demand for taxi services is maintained within the Canberra Cabs network system. This provides detailed information, particularly in regard to telephone bookings through the network. From this information, demand for rank and hail bookings may be estimated, ie total bookings on the network less phone bookings. In practice, the 'rank and hail' figure includes bookings made through informal mobile phone networks, ie some taxi drivers may have regular users who book a taxi using their mobile phones. This market is likely to be small.

Weekly telephone booking demand for taxi services shows some variability. Figure 5.1 shows the pattern of weekly radio bookings demand for Canberra Cabs' network during 1999 and 2000. The data shows no growth over the two years. The variability for each year follows a similar pattern.

Figure 5.1 Trend in weekly demand for telephone bookings



Source: Canberra Cabs.

In 1999, highest demand was experienced in November and early December, peaking at 40,308 bookings for a week in November. For the November-December period in 2000, peak demand was recorded in early December at 36,146 bookings. However, for the year 2000 overall, peak demand occurred in June at 38,526 bookings.

Demand drops off considerably in January, coinciding with the major school holidays of the year. Other school holiday periods of the year are also associated with falls in demand, although the extent of those falls is moderate compared to the January period. Overall, demand for taxis generally ranged between 30,000 and 38,000 telephone bookings per week for the year 2000.

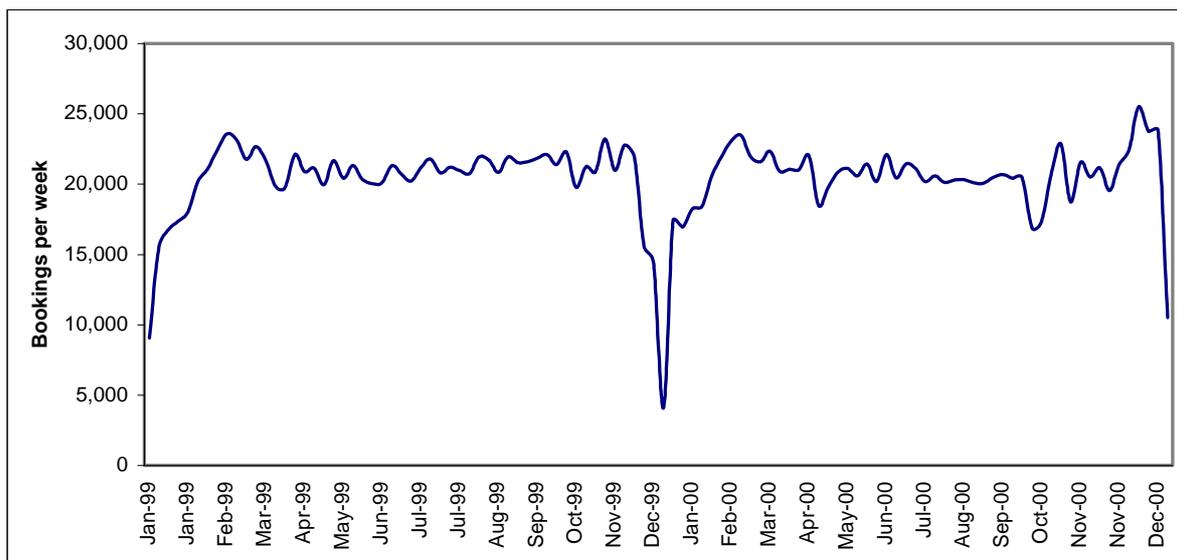
In the year 2000 there is a clear 'break' in demand between the first and second halves of the year. Demand fell through July of that year, possibly associated with school holidays, and did not fully recover when compared to the experience of 1999. One possible explanation for this is the impact of the Olympics, particularly during September and early October when a considerable fall in demand is evident. It appears that business activity was reduced due to the Olympics, and this had a significant effect on taxi demand. It is possible that demand for 2001 will return to a pattern and level similar to that for 1999.

Figure 5.2 illustrates weekly demand for 'rank and hail' bookings. The pattern of demand is similar to that for radio bookings, ie relatively high in November and early December of each year, with January showing a significant fall. The period associated with the Olympics is also associated with a sharp fall in demand. Unlike telephone demand, 'rank and hail' bookings show relatively strong demand over February and March of each year. This may be associated with the influx of university students during that period.

The figure indicates that rank and hail demand increased strongly in the weeks leading up to Christmas 2000, compared with demand in 1999. Closer inspection of the data indicates that although both telephone and rank and hail hirings fell between 1999 and 2000, there was a relative shift to rank and hail bookings. The percentage fall in rank and hail bookings was less than that for telephone bookings.

Figures 5.1 and 5.2 indicate that telephone bookings contribute the greatest share of total demand. Telephone bookings represent around 60 per cent of all bookings.

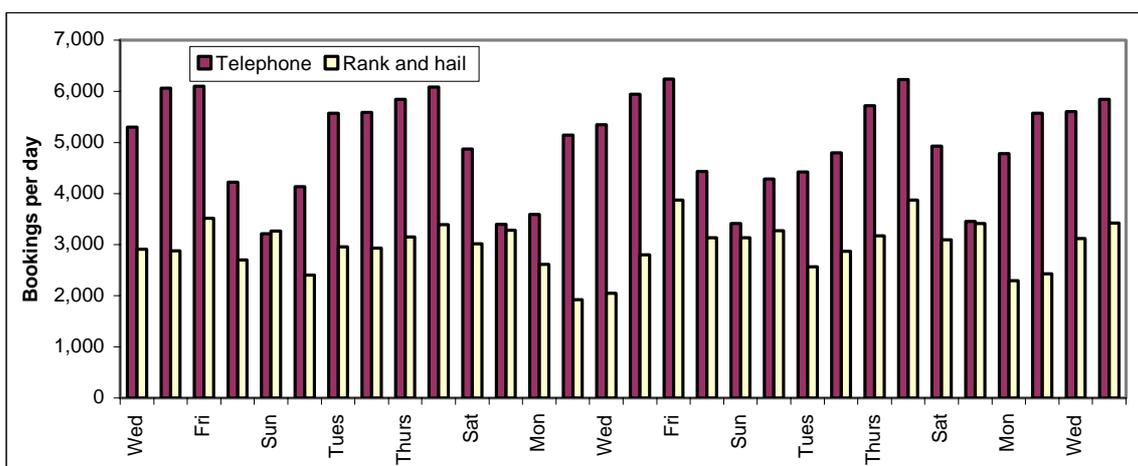
Figure 5.2 Trend in weekly demand for ‘rank and hail’ bookings



Source: Canberra Cabs.

Figure 5.3 shows the pattern of daily bookings for telephone and rank and hail demand.

Figure 5.3 Daily booking totals– November 2000

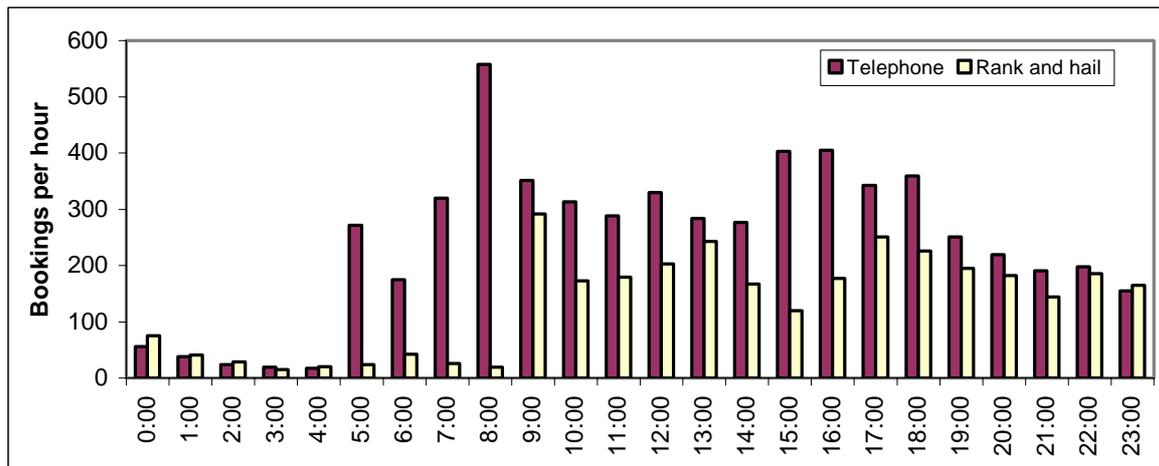


Source: Canberra Cabs.

Figure 5.3 illustrates a consistent pattern in terms of increasing demand for telephone bookings over the latter part of each week, with demand highest on Thursdays and Fridays. The pattern for rank and hail bookings is not as consistent, but highest demand also tends to occur on Fridays. Sundays also show relatively high demand, in contrast to the telephone bookings market.

Figure 5.4 shows how hourly demand for both telephone and rank and hail demand varies over a typical weekday.

Figure 5.4 Hourly booking totals on weekday – 9 Nov 2000

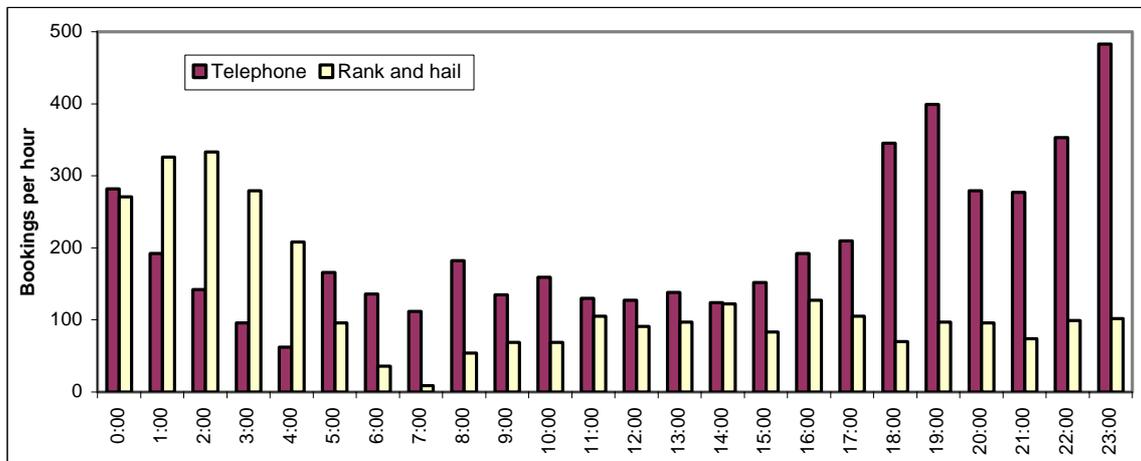


Source: Canberra Cabs.

The general pattern of demand is similar. Peaks occur between 8:00 and 10:00am, and 3:00 and 7:00pm. The demand is mostly for telephone bookings.

Figure 5.5 shows how hourly demand varies over a typical weekend day for both telephone and rank and hail demand.

Figure 5.5 Hourly bookings totals on weekend day – 11 Nov 2000



Source: Canberra Cabs.

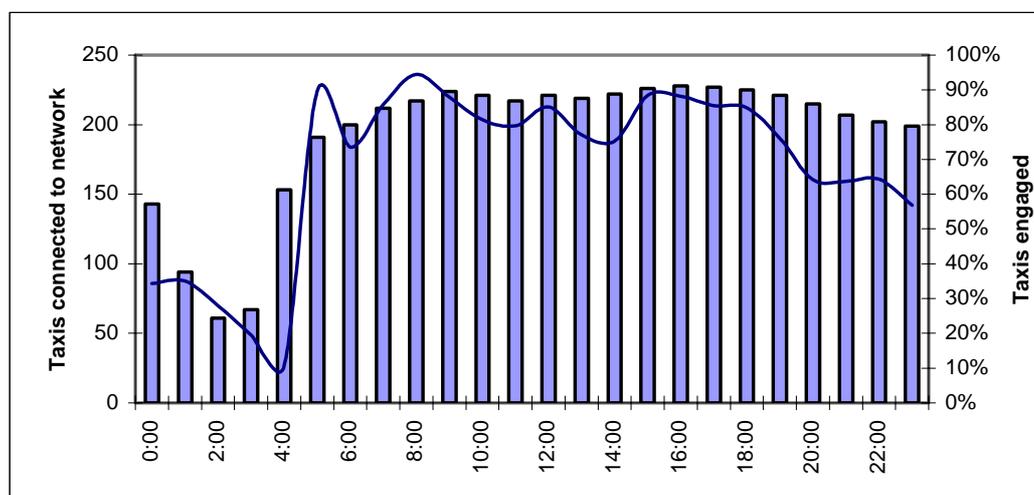
Demand patterns for the two services are quite different. Telephone bookings are greatest from 6:00pm to 12:00am, consistent with customers using taxis to go out for the evening. Rank and hail demand peaks in the early hours of the morning, as customers use taxis to return home after an evening out. The central location of many restaurants/night spots in Canberra with taxi ranks nearby contributes to this outcome.

The figures indicate significantly different demand patterns between weekday and weekend. For the weekday, there is very low demand in the early hours of the day, with demand peaking around the start and end of the working day. In contrast, for Saturday 11 November 2000, demand peaked between 6:00pm and 12:00am for telephone bookings, and between 12:00am and 5:00am for rank and hail demand. During the weekend demand for both telephone and rank and hail bookings is relatively low compared to weekdays.

As the above figures illustrate, demand varies on a daily, weekly and yearly basis. The taxi industry/operators have to manage their service provision to meet this varying demand. In periods of high demand, a relatively higher number of taxis is likely to be connected to the network, and similarly with the proportion of taxis engaged, ie occupied. During low demand periods, the opposite is likely to be the case because taxis will be on the road only if the operators believe they will make money during that time period.⁸

These issues are illustrated in figures 5.6 and 5.7, and considered further in section 5.4.2.

Figure 5.6 Number of taxis connected to network and % engaged – 9 Nov 2000



Source: Canberra Cabs.

The line across figures 5.6 and 5.7 indicates the proportion of taxis connected to the network at that time that are engaged, as measured on the right hand scale. The columns indicate the number of taxis connected to the network.

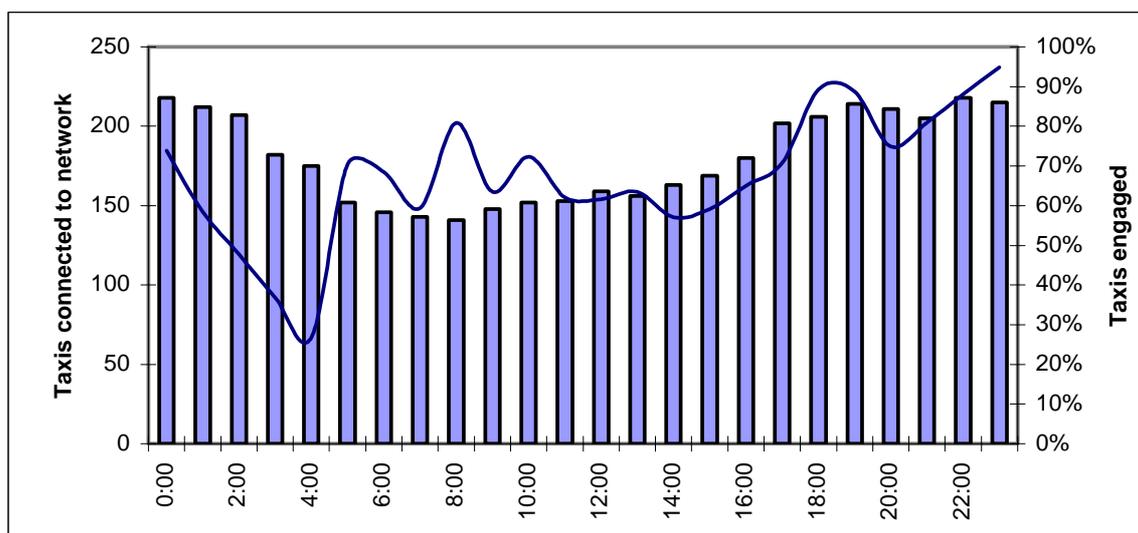
The pattern for number of taxis connected to the network is generally consistent with daily demand, insofar as a low number of taxis is connected during the early hours of the day. For the remainder of the day, there are a consistently high number of taxis connected, usually between 190 and 225. The number slowly decreases towards the end of the day.

⁸ During the period to which these figures relate, there were 233 taxi licences in the ACT. These were split between standard taxis (217) and WATs (16). The ACT has since released an additional 10 WAT licences.

The variability of taxis engaged is consistent with the pattern of hourly demand (figure 5.5). Where demand is low or decreasing, the proportion of taxis engaged tends to be low and/or falling. This is particularly evident during the early and late hours of the day. To a very limited extent, the managing of taxi supply by operators does moderate the variability in taxis engaged. Fewer taxis are connected to the network in the early hours of the day. However, as the figure illustrates, the increase in taxis connected at 4:00am, without a commensurate increase in demand, results in the proportion engaged falling sharply at that time. Similarly in the late evening, the decline in taxis connected to the network does not keep pace with decreasing demand, resulting in a sharp fall in the proportion of taxis engaged from around 6:00pm.

For a significant period of the day, the proportion of taxis engaged is over 80 per cent. This is a relatively high figure when compared to taxis in Sydney, where the proportion engaged does not reach 80 per cent even during peak periods.⁹ Notwithstanding the different market factors in Canberra and Sydney (eg traffic conditions/congestion), this suggests that the ACT market has a low number of taxis relative to demand.

Figure 5.7 Number of taxis connected to network and % engaged – 11 Nov 2000



Source: Canberra Cabs.

As in figure 5.6, the number of taxis connected to the network shows a similar pattern to demand. However, changes in taxis connected is not sufficient to compensate for changes in demand. Hence, the proportion engaged shows sharp variability, particularly in the early morning and late evening. This is particular true in the late evening, when the proportion of taxis engaged reaches 95 per cent. Again, this is a very high result when compared to Sydney.

The information in figures 5.6 and 5.7 may have relevance and importance in relation to waiting times. Waiting times are influenced by the proportion of taxis engaged, which in turn is a function of demand and number of taxis on the network.

⁹ IPART, *Review of the taxi cab and hire car industries*, Final Report, 24 November 1999, pp 37-38.

5.4.2 Waiting and response times

Under the existing MoU Canberra Cabs is required to report quarterly on waiting time and response time performance. The MoU requires that Canberra Cabs have its records and quarterly reports audited by an independent auditor. The Commission is aware that to date this has not occurred, and the ACT Government has not enforced this requirement.

The following tables show Canberra Cabs' recent performance in relation to the MoU requirements:

Table 5.1 Waiting times: 3 – 6pm Monday to Friday

MoU requirement	Sep 00	Jun 00	Mar 00	Dec 99
Standard				
85% < 18mins	99.7	99.0	96.3	96.7
95% < 30 mins	98.4	96.0	98.9	98.8
WAT				
85% < 18mins	72.4	66.2	89.5	86.8
95% < 30 mins	87.9	87.8	96.6	93.0

Table 5.2 Waiting times: all other times

MoU requirement	Sep 00	Jun 00	Mar 00	Dec 99
Standard				
85% < 10mins	87.7	86.2	86.6	86.6
95% < 20 mins	99.2	98.6	98.9	98.5
WAT				
85% < 10mins	63.0	60.1	81.8	79.3
95% < 20 mins	86.3	84.1	94.7	94.2

Performance is differentiated for standard and WATs, and a distinction is made between 3:00 – 6:00pm Monday to Friday, and 'all other times'. The time period between 3:00 – 6:00pm Monday to Friday is a peak demand period, and performance requirements are different (relatively lenient) for these times.

Standard taxis

Performance for standard taxis generally meets the MoU requirements. For the period 3:00 – 6:00pm Monday to Friday, Canberra Cabs has easily achieved the performance requirements. This is also the case for the performance requirement that 95 per cent of telephone booking customers wait less than 20 minutes at 'all other times' (table 5.2).

Interestingly, performance requirements are barely achieved for 85 per cent of telephone booking customers having to wait less than 10 minutes at 'all other times', ie during periods outside the peak demand times of 3:00 – 6:00pm Monday to Friday.

This outcome suggests that:

- peak period performance requirements for standard taxis could be tightened. Performance targets that are achieved by default do not provide incentives to

continually improve. This suggests a gradual convergence between peak and off peak performance requirements

- the indicators do not properly reflect peak periods. Certainly, the information presented in the figures above suggests multiple peaks in the Canberra taxi market. The fact that Canberra Cabs' performance requirements are easily met at 'all other times' suggests that a convergence of performance indicators between current peak and off peak periods may be warranted.

As well as the general pattern that demand tends to follow on a daily, weekly and yearly basis, increased demand (or conversely tight supply) may occur randomly throughout the day due to particular circumstances. This differs from the general peaks and pattern of demand identified above.

The Commission notes that Canberra Cabs has put in place processes to meet these demand 'hot spots'. The system has been trialed since February 2001, and involves identifying hot spots through the network system, and directing drivers to those areas. The network operator remunerates the driver for attending that particular area. The Commission views this as a good example of the network operator providing innovative services in order to maintain/improve service levels.

Wheelchair accessible taxis

Canberra Cabs' performance in relation to WATs is more variable than for standard taxis, and generally does not meet the requirements of the MoU.

During the peak period 3:00 – 6:00pm Monday to Friday, the MoU requires Canberra Cabs to have 85 per cent of its customers experience a waiting time of no more than 18 minutes. Between December 1999 and September 2000, performance ranged between 66.2 per cent and 89.5 per cent, with the requirements met in only two out of the four quarterly periods.

Canberra Cabs' performance in relation to 95 per cent of its customers experiencing a waiting time of no more than 30 minutes between 3:00 – 6:00pm Monday to Friday is closer to the standard required by the MoU, but still generally falls short. Between December 1999 and September 2000, performance ranged between 87.8 per cent and 96.6 per cent, with the requirements being met on only one occasion during the four quarterly periods.

During 'all other times', Canberra Cabs' performance did not meet the requirements of the MoU on any occasion. In relation to the target of 85 per cent of customers waiting less than 10 minutes, performance ranged between 60.1 per cent and 81.8 per cent. For the target of 95 per cent of customers waiting less than 20 minutes, performance ranged between 84.1 per cent and 94.7 per cent.

Response times

The Commission has considered the response time information that Canberra Cabs submits on a quarterly basis. Generally, response times for standard taxis are 'front loaded' into the less than 5 minutes and 5-10 minutes categories, ie a significant majority of standard taxi customers wait less than 10 minutes for a taxi. The majority of WAT response times is in the less than 5 minutes category, although the degree of 'front loading' is far less compared to standard taxis, ie the average waiting time for WAT users is greater than for standard taxi users.

This again suggests that service levels for users of WATs is relatively poor. Waiting time targets for WATs are generally not achieved, and on average, response times are higher than is the case with standard taxis.

The Commission notes that the ACT Government has recently released an additional 10 WAT licences. These are expected to begin operation around the middle of 2001. This should assist in improving service levels to WAT users. The ACT Government has also stated its intention to strengthen the enforcement of WAT licence requirements. In its response to the Freehills report (see section 6.4), the ACT Government notes that the September 2000 quarterly waiting times report indicates that 28 per cent of WAT hirers waited more than 18 minutes. In contrast, only 0.3 per cent of standard taxi hirers waited more than 18 minutes.

The Commission understands that the ACT Government is considering incentives for WAT operators, eg specific charges to reflect the additional costs of providing a WAT service. A combination of appropriate incentives as well as strengthening the enforcement of WAT licence conditions should improve service levels to WAT users.

Finally, the MoU requires that no zone within the Canberra Cabs network should have more than 40 per cent of hirers waiting more than 10 minutes. For each of the periods above, this requirement was not met for zone 20, the suburb of Hume. However, Canberra Cabs notes that this area accounts for less than 1 per cent of all hirings, and that over 80 per cent of hirers have a waiting time of no more than 15 minutes.

5.5 Taxi industry survey

The Commission is interested in assessing a broad set of information that encompasses other service issues in addition to waiting times. When considering service quality there are a range of factors that need to be taken into account. These include vehicle cleanliness and condition, driver courtesy, street knowledge and driver ability.

The ACT Government has conducted two annual surveys of the Canberra taxi industry. The second survey, for the year 2000, was released recently. The survey collects information on industry performance and a broad range of service quality issues, including users' perceptions of service levels. As well as collecting information on waiting times similar to the quarterly reports required under the MoU, additional information includes:

- customer waiting times at taxi ranks
- taxi waiting times at taxi ranks
- assessment of driver performance
- assessment of some aspects of the taxi vehicle
- customer assessment of quality of service
- survey of customers from Canberra Airport.

The key findings of the survey are:

- waiting/response times for standard taxis have increased across the board from 1999, ie for telephone bookings and taxi ranks (waiting times for WATs were not surveyed in 1999)
- the target that 85 per cent of telephone booking customers wait no more than 10 minutes during off peak times has not been achieved. For standard taxis the response time achieved was 12:53 minutes, and for WATs, 23:08 minutes¹⁰
- peak period waiting time requirements have been achieved for both standard taxis and WATs (this result for WATs contrasts with some of the information in the MoU quarterly reports)
- response times in certain off peak periods were longer than those in the general off peak time, specifically in the 7:30am – 9:30am period
- telephone booking waiting time targets for WAT services in off peak periods have not been achieved
- although customer waiting times at taxi ranks have increased (in some cases significantly, eg 100 per cent), they are still within the waiting time requirements specified in the MoU for telephone bookings
- drivers of WATs provide a reasonable level of service, but the following require attention:
 - securing chair and passenger to an adequate standard, and knowing and acknowledging the specific needs of WAT passengers is a matter for training
 - at what point of the journey the taxi meter should be started
 - defining the extent of the service to be provided, eg assistance in gaining access to buildings. Respondents were divided on whether this should be part of the service provided
 - design issue in terms of passengers’ ability to see the taxi meter from their seated position
- surveyors encountered a small number of instances where drivers were being dishonest or were inadvertently making mistakes:
 - on two occasions surveyors were overcharged by a factor of 200 per cent, by the cost of the journey also being included as the ‘tip’ on a cabcharge docket. If being dishonest, this could be explained away as a fault of the machine
 - the fare rate was set incorrectly for the time of day
 - on two occasions the meter was started before the driver made contact with the surveyor.

¹⁰ Note, the quarterly reports viewed by the Commission indicate that Canberra Cabs just achieved the performance requirement that 85 per cent of standard taxi customers wait no more than 10 minutes. The MoU information indicates that the requirement for WATs was not achieved.

5.5.1 Quality of service survey

Three survey methodologies were applied to assess service quality: telephone, face-to-face with users at Canberra airport, and an on-board survey. Aspects of service quality assessed included:

- response time
- driver ability
- driver's knowledge of Canberra
- accuracy of the fare charged
- handling of cash or cabcharge by driver
- driver courtesy
- cleanliness and condition of the vehicle.

The survey indicates that users are generally happy with the level of service provided in regard to the above. For each of the factors, at least 80 per cent of users were either satisfied or very satisfied with the service provided.

This outcome is consistent with the quarterly waiting time information supplied through the MoU. This data suggests that for standard taxis, waiting time requirements have been achieved. Interestingly, the taxi industry survey indicates that even though the 85 per cent waiting time requirement for off peak periods was not achieved, most users expressed satisfaction with the service provided. This may suggest that although the waiting time target was not achieved, the average waiting time was considered reasonable by the respondent.

The high level of satisfaction with service standards is a positive outcome. However, such an outcome does not support continued regulation of the industry through licence quota restrictions. It is an indication that current service standards are high. It is not an indication that users would not accept a lower standard of service, in conjunction with a lower fare.

The Commission is not recommending that current service standards be allowed to fall. Within guidelines set by the Government and industry, appropriate levels of service should be provided. As discussed in the following section, customer satisfaction and service standards can be maintained in a deregulated environment.

5.6 Service quality and deregulation

Regulation of the taxi industry is often justified on the grounds that in an unregulated environment quality standards would suffer, with the cost of such a deterioration borne by rank and hail customers who have little ability to pick and choose between taxis.

Sections 5.4 and 5.5 have considered the recent performance of the ACT taxi industry. Areas have been identified where service quality may be poor and/or decreasing. Aspects of service quality where positive customer sentiment exists have also been identified.

The unanswered question at this stage is what happens to service standards in an unregulated environment.

Proponents of continuing regulation often regard deregulation as an ‘all or nothing’ decision. They claim deregulation of quota restrictions, service standards, fare levels, etc would lead to a proliferation of new entrants, and service standards would fall as taxi operators competed for a fixed (in the short term at least) number of customers.

However, deregulation of the industry need not take this path. Once quota restrictions have been removed, the relevant government can still maintain a role in setting service standards, in authorising/licensing networks, operators and drivers, and in monitoring service provision. Government will maintain the power to sanction industry participants where necessary.

Enforcement of such requirements can produce positive outcomes by maintaining service quality. Rank and hail customers will always be in a relatively adverse position compared to phone booking customers, when considering the impacts of deregulation. However, the relative position of rank and hail customers should not be confused with their absolute position. In absolute terms, they may still be receiving an appropriate level of service. If there are strong concerns in regard to deregulation’s effect on such customers, stringent enforcement of service standards will alleviate those concerns.

It should be kept in mind that a key advantage of competition and deregulation is that consumer choice is generally increased. Service providers may choose a particular position on the service quality/price trade off, consistent with government requirements in regard to minimum service quality standards. Further, regulation of **maximum** fares can be maintained by government in a ‘deregulated’ market.

With appropriate safeguards, the Commission considers that the removal of licence number restrictions can promote community benefits while maintaining service standards in a deregulated environment.

6 COMPETITION POLICY

6.1 Conclusions

There are a range of competitive restrictions present in the taxi industry. These are identified in state/territory and federal reviews of the industry, including that of Freehills (see section 6.4 below) on the ACT taxi industry. Competitive restrictions affect the efficiency of the industry.

The Freehills report identifies significant efficiency losses associated with quota restrictions. Competition would remove these losses. It would also encourage taxi operators to minimise their costs, while meeting service level requirements.

The ACT Government has responded to the Freehills report. In particular, it has stated that no additional standard taxi licences will be issued, pending a further review of the industry prior to June 2002. An additional 10 WAT licences have been released.

Of relevance to the ACT Government's approach to reform is the recent release of the National Competition Council's *Framework for the third tranche assessment of government's progress with implementing national competition policy and related reforms* (see section 6.5 below).

The NCC states that proposals for a transitional approach to reform must be accompanied by rigorous public interest justifications. The ACT Government is proposing a further review of the industry prior to a final decision on the removal of taxi licence quotas. This review would need to identify the public interest justifications if quota restrictions are to remain in place.

In relation to fare regulation, Freehills recommends that until adequate new entry has occurred (following the removal of entry restrictions), maximum fare regulation should be maintained. The ACT Government agrees with this, stating that the Commission should maintain its role of fare regulation and that operators continue to be allowed to charge below the maximum fare. The Commission generally agrees with this approach.

However, the Commission notes that particular care must be taken in applying a pricing methodology to set maximum fares in a market where licence quota restrictions are removed. For example, under the new pricing approach which calculates a surplus/deficit figure, an increase in taxi numbers without an increase in demand would result in reduced average takings per taxi. This would translate into a fare increase, other things being equal. This would be a perverse outcome, competition leading to fare increases. If quota restrictions are removed and maximum fare regulation maintained (at least initially), the Commission would be careful to avoid any inappropriate pricing outcomes.

Recommendation 4 – Fare regulation

The Commission recommends maximum fare regulation be initially maintained when and if licence quota restrictions are removed. If removed, the response of industry should be monitored to determine the requirement for continued maximum fare regulation.

Freehills recommends that consideration be given to establishing an additional network operator in the ACT. The ACT Government is pursuing this proposal, and has called for

tenders to offer such a service. The Commission generally supports the establishment of a second network operator in the ACT, but is concerned with the approach that the ACT Government may adopt.

Firstly, the full benefits of reform are unlikely to be achieved under a piecemeal approach. The benefits of an additional network operator will not be fully realised in an environment where licence quota restrictions exist. Secondly, the Commission considers that during the introduction of a new network operator, enforcement of performance standards should reflect the ACT Government's obvious aim of establishing the operator. Some flexibility, as appears to have been taken with the incumbent network operator, should be applied where service requirements have not been achieved.

Recommendation 5 – Taxi networks

The Commission recommends that the ACT Government act to encourage the establishment of an additional taxi network service provider. This may be reflected in the assessment of performance against stated requirements.

6.2 Introduction

The terms of reference for this review require the Commission to consider the 'degree of competition within the industry and the way in which that may affect the efficiency of the industry'.

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

The reform package includes a commitment from all the Australian Governments to review and reform any legislation which might restrict competition and which is not in the public interest. The general principle is 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 legislation can be achieved only by restricting competition.

The ACT Government has reviewed legislation relating to the taxi and hire car industries. The Commission has considered the outcomes of this review and the ACT Government's response to the review, in fulfilling its own requirements under the terms of reference.

Conclusions from the ACT Government review in relation to the taxi industry are presented below in section 6.4.

6.3 Competition and efficiency

Economic theory suggests that in a competitive environment, the interaction between service providers and consumers is likely to produce efficient outcomes (eg fares levels, service quality). In a deregulated market, if the cost of offering a service is greater than the amount consumers are willing to pay, the service will not be offered, or will be withdrawn to avoid a loss for the providers of the service. If a service provider is charging an excessive price,

another provider may enter the market, charge a lower price, and win consumers from the previous supplier.

When prices and service levels are set through competition, resources in the economy tend to be allocated to their best uses (allocative efficiency). Competition tends to result in the least cost/most efficient service providers serving the market (productive efficiency). Competition plays a dual role in the economy, promoting both allocative and productive efficiency.

Of course, competition does not work perfectly and may not always be feasible. However, it provides a process whereby misjudgements by producers regarding the cost of production, price or quality of service, may be corrected. If a service provider seriously misjudges what the market wants, it will be worthwhile for another producer to enter the market. Sooner or later, such entry will take place. On the other hand, regulation may lock in excessively high costs or inappropriate services for long periods.

In the context of the ACT taxi industry, government regulation of licences severely limits the number of operators in the market. No standard taxi licences have been issued since 1995. This limitation on supply is one factor that has seen service providers not depart from the regulated maximum fare. In effect, the regulated maximum fare is the only fare available. This is also recognised in the Freehills report (see following section). Competition has been constrained through supply restrictions.

The removal of supply restrictions need not imply reduced service levels and/or fare exploitation. Removal of supply restrictions can co-exist with maximum fare regulation and minimum service quality requirements. The industry competition that eventuates may involve service providers offering fares below maximum fares in an effort to attract customers, and varying service levels, which would have to meet the required minimum service standards as required by the ACT Government. Such a process would see consumer choice increased. Those service providers and service level combinations that survived would be the most efficient providers, offering a service demanded by the community. These market mechanisms cannot operate effectively in the current regulated environment.

Taxi operators are currently limited in the supply of network services. There is only one provider of network services in the ACT. The competition arguments concerning taxis/consumers, can equally relate to network operators/taxi operators (specific discussion on these issues is contained in section 6.6).

6.4 Freehills report

Under the National Competition Policy reform package, the ACT Government has agreed to review, and where necessary, reform all existing legislative restrictions on competition. Independent consultants Freehills Regulatory Group (Freehills) were appointed by the ACT Government to review the ACT's taxi and hire car legislation. A final report by Freehills was completed in March 2000.¹¹ Public release of the report was on 15 November 2000.

¹¹ Freehills Regulatory Group, *National competition policy review of ACT taxi and hire care legislation*, Final Report, Prepared for ACT Department of Urban Services, March 2000.

Key findings of the review are:

- licence quota restrictions do not address legislative objectives and impose substantial costs on consumers and potentially on other industry participants such as drivers
- the provisions create a transfer of wealth from consumers to licence owners and lessees. The quota restrictions inflate the value of licences, reduce potential total hirings and raise fare levels. The transfer of wealth from consumers to taxi licence owners is estimated at around \$5.6m per annum
- regulations which directly address driver, operator and vehicle standards generally have significant benefits in the form of higher consumer, driver and public safety, and in improved quality of service.

Given the key conclusions of the review as above, options for reform of the industry were considered by Freehills. The review presents the following options for taxi licence quotas:

- removing taxi quota restrictions
- phasing in additional taxi licences
- no reform to current taxi licence numbers
- introducing an additional category of licences to operate during peak times only.

The Freehills report notes that reform of taxi regulations has been approached differently in many jurisdictions with divergent results. It is therefore difficult to conclude which approach would provide maximum benefits for the community. Nonetheless, Freehills has recommended that the removal of taxi quota restrictions would be the preferred approach to licence quota reform.

The Freehills report notes that each of the above options has different implications for the issue of compensation. For instance, an immediate removal of all quota restrictions would create a strong case for compensation for the loss in licence value. Freehills concludes that for reasons of pragmatism and equity, compensation should be given where substantial losses occur due to policy changes.

6.4.1 ACT Government response

In December 2000, the ACT Government formally responded to the Freehills report. Recommendations and the Government's response for areas particularly relevant to the Commission's review are presented below:

Licence quota restrictions

Freehills stated a preference for removing taxi quota restrictions completely.

Government response: the Government prefers a transitional response to licensing. As a first step, the Government immediately released ten WAT licences to ensure response times for WATs are equivalent to those applying to standard taxis.

At this stage the Government does not see a need to release additional standard taxi licences. It proposes to review these arrangements, community needs and industry viability before June 2002.

The review team (ie Freehills) has expressed the view that where individuals incur substantial loss as a result of policy changes resulting in the removal of licence quotas, a case for compensation may exist. The Government considers that there is no statutory or other legal entitlement for compensation.

Wheelchair accessible taxi licences

Freehills recommends that the regulator retain the power to set a minimum level of supply of WAT licences governed by minimum response times equivalent to standard taxis and that direct or explicit subsidies be given to WAT licence holders/operators or consumers to achieve those levels of supply.

Government response: agrees. The Government has made a commitment to ensure people in wheelchairs have access to a taxi service with a response time at least as good as for standard taxis. Response times will continue to be closely monitored. WAT operators are required under the conditions of their licence to give priority to people in wheelchairs. Those operators who fail to comply with licence conditions may be fined or have their licence suspended or cancelled.

Options for providing direct or explicit subsidies for service will be examined as part of the further review to be completed within the next 18 months.

Issuing licences

Freehills recommends that the role of the regulator (ie ACT Department of Urban Services) in attempting to balance supply and demand should be removed. Instead, the regulator should issue licences on demand subject to the applicant satisfying the appropriate licence holder and operator accreditation provisions, vehicle safety requirements, and payment of an appropriately costed annual licence fee.

Government response: agrees in principle. The Government does not intend to remove taxi licence quota restrictions at this time. However, as regulator, it will give greater emphasis to licence and operator accreditation processes and vehicle safety requirements under the proposed new legislation.

Fare regulation

Freehills recommends that in the context of removing the legislative restrictions on supply, fare setting powers should be replaced with a fare approval regime for accredited taxi companies. In order to protect against price exploitation, the current maximum fare should remain the maximum until adequate new entry has occurred. If ongoing maximum fare regulation of taxis is retained, consideration should be given to including additional factors in the methodology to attempt to achieve more efficient pricing, eg factors to account for benchmarking or change of interstate prices, technology, productivity, cost of capital, driver earnings and/or demand elasticities.

Government response: agrees that maximum fares should continue to be regulated as this will reduce price exploitation and prevent haggling on prices that could lead to disorder at ranks or on the street. The Government proposes that maximum taxi fares continue to be determined by the Commission and that taxi operators remain free to choose to charge a lower fare.

Taxi network requirements

The principal network contract requirements should include 24 hour 7 day a week booking services, complaint handling procedures, public liability insurance coverage, and at least during the initial years of reform a minimum of 15 taxis per network. For non dominant networks, minimum response time standards should be removed or reduced sufficiently to permit new entry at the network level.

Freehills recommends that consideration be given to proposals, such as that put by Queanbeyan Taxis, to establish a competing network in the ACT in order that an important source of competition to the Aerial [Canberra Cabs] network may emerge.

Government response: the Government recognises that competition at the network level is important to the maintenance and improvement of service standards including a reduction in waiting times. Competition should lead to innovation, lower network fees and a greater choice for customers.

The Government proposes experienced or otherwise qualified organisations be encouraged to establish an additional taxi network in the ACT. Until network accreditation arrangements have been settled, the introduction of an additional network will be invited on similar terms and conditions to those applying in the Government's agreement with Canberra Cabs.

Cross border restrictions

Freehills recommends that the ACT Department of Urban Services and the NSW Department of Transport enter discussions with a view to establishing a single taxi regulatory regime for the region. Consistent with IPART's recommendations that the regulation of the NSW regional taxi sector be devolved to local councils¹², the ACT legislation would be regarded as the preferred governing legislation. In the interim, the two regimes should give full mutual recognition to the respective licence holders.

Government response: agrees. Discussions have commenced between the two government departments.

The above issues and the ACT Government's response are considered further in section 6.6.

6.5 National Competition Council

The National Competition Council (NCC) was established on 6 November 1995 by the *Competition Policy Reform Act 1995* following agreement by the Commonwealth, State and Territory Governments. A federal statutory authority, it functions as an independent advisory body for all governments on the implementation of national competition policy.

In order to ensure gains from reforms are shared across the community, the Commonwealth makes national competition policy payments to each state and territory. The pre-requisite for receipt of full payments is that the state and territories make satisfactory progress on the agreed reform agenda.

¹² See IPART, *Review of the taxi cab and hire car industries*, Final report, November 1999, p 86.

It is the NCC's task to assess progress on meeting the reform agenda. It may recommend the Federal Treasurer reduce payments to a state or territory if that state or territory has not implemented reform in the public interest. The NCC has commenced its third tranche assessment on the implementation of national competition policy reform.¹³ Key aspects of the NCC's commentary on the taxi industry follow.

The NCC notes the common approach to regulation of the taxi industry that has been taken historically across Australia. Two broad types of regulation have co-existed. Firstly, jurisdictions have imposed regulation of standards, such as age and road worthiness of vehicles, and entry requirements for drivers. These are essentially aimed at passenger safety issues. Secondly, jurisdictions have severely limited the number of taxis in the market. Fare regulation has accompanied entry restrictions.

The regulation of quality standards does not have a substantial impact on competition. However, the NCC states that entry restrictions, together with fare regulation, have significantly restricted competition in all jurisdictions.

The NCC's third tranche assessment framework identifies key areas that it will focus on in its assessments in June 2001 and June 2002. The taxi industry is one such area identified by the NCC.

6.5.1 Review and reform activity

Each of the states and territories has reviewed the regulation of its taxi industry. However, the NCC notes that no major reform has been implemented to date in any jurisdiction other than the Northern Territory.

Table 6.1 Review and reform activity

Jurisdiction	Review completed	Recommendations	Reform activity
NSW	Nov 1999	5% annual increase in licences (restricted, non transferable) 2000 – 2005 Further review 2003 Continue fare regulation	Release of additional licences in train Initial problems with take up due to high asking price Performance reviews established
Victoria	July 1999	Remove entry restrictions Buy back existing licences, funded by annual fees on operators Retain fare regulation pending development of competitive market Improve quality of fare regulation by transfer of responsibility to an independent economic regulator	Victoria has advised that it is currently developing its response to the review

¹³ National Competition Council, *Framework for the third tranche assessment of governments' progress with implementing national competition policy and related reforms*, AusInfo, Canberra, 5 February 2001.

Independent Competition and Regulatory Commission

Jurisdiction	Review completed	Recommendations	Reform activity
Queensland	publicly released Sep 2000	Revamp regulatory structure around performance agreements with booking companies Allow booking companies control over licence numbers	None
WA	Aug 1999	Remove licence restrictions Use substantial training requirements to regulate entry Full compensation to existing plate owners New licences issued at maximum rate of 20% pa on first come, first served basis	Tenders called for release of limited number of restricted licences (peak period and multi purpose)
SA	review completed late 1999	Retention of existing restrictions (the Act allows 5% new licences pa, though none have been issued) Reliance on competition from hire cars, with removal of some current restrictions	None
Tasmania	final report Apr 2000, not publicly released	5% new licences annually, or 10% if tender price exceed valuations by 10% Maximum fare retained for rank and hail market only	None
ACT	final report finished Mar 2000. Report considered by Cabinet Oct 2000	Immediate removal of restrictions on supply of taxi licences Full compensation to licence holders Compensation funded via consolidated revenue or by long term licence fee regime	None
NT	discussion paper released May 1998	Restrictions on licence numbers eliminated Compensation paid as lump sum Substantial licence fees to recoup compensation costs Maintenance of fare regulation	Recommendations implemented January 1999

Source: adapted from National Competition Council, *Framework for the third tranche assessment of governments' progress with implementing national competition policy and related reforms*, AusInfo, Canberra, 5 February 2001, pp 11.2-11.3.

All the reviews generally state that entry restrictions do not provide net benefits to the community, or that net costs to the community are incurred. A key concern for the NCC is that where removal of restrictions is recommended, details of the expected or recommended reform path have not been provided.

Given the conclusions reached in each of the reviews, the NCC states that any proposal to retain restrictions on licence numbers must be accompanied by rigorous public interest justifications. This also applies where extended transitional arrangements are proposed. The NCC would also be concerned where alternative mechanisms acted to limit entry to the industry, for example, **substantial** training requirements. These would also need to meet the net community benefit test.

For the ACT, taxi licensing has been identified as a key area of concern. The NCC has stated that failure to progress reform is likely to be regarded as a substantial failure of compliance with national competition policy objectives.

The NCC concludes by saying:¹⁴

These factors suggest that most jurisdictions still need to make significant further progress in order to meet NCP [national competition policy] obligations in regard to the taxi industry. They also suggest that non-compliance on taxi regulation would be likely to be regarded as a substantial failure of compliance with overall legislative review commitments.

Public interest and net community benefit

In order to justify continued regulation, rigorous assessment on public interest grounds must take place, and a net community benefit from continued regulation should exist. These two factors are really separate statements of the same requirement. For regulation to be maintained there must be a net community benefit, this is the *public interest* test.

Under the Competition Principles Agreement signed by state/territory and federal Governments, legislation reviews state that:

The guiding principle is that legislation (including Acts, enactments, Ordinances or regulations) should not restrict competition unless it can be demonstrated that:

- (a) the benefits of the restriction to the community as a whole outweigh the costs; and
- (b) the objectives of the legislation can only be achieved by restricting competition.

Part (a) specifically identifies the 'net community benefit' requirement as justification for continued regulation. National competition policy has a community wide perspective, rather than a focus of particular groups. This implies that for restrictions to be maintained they must be shown to benefit the community as a whole. This does not preclude consideration of impacts on individuals, regions or industries exposed to reform. The Council of Australian Governments (CoAG) has agreed that in examining public interest issues in relation to national competition policy reform, governments should give consideration to identifying the likely impact of reform on specific industry sectors and communities.

CoAG has directed governments to document the public interest reasons supporting a decision/assessment, and to make these available to interested parties and the public.

One factor that the numerous federal and state/territory reviews of the taxi industry have not considered in detail is the payment of compensation, or more precisely, the raising of

¹⁴ National Competition Council, *Framework for the third tranche assessment of governments' progress with implementing national competition policy and related reforms*, AusInfo, Canberra, 5 February 2001, p 11.5.

funds to pay for compensation. Where compensation is paid by government, either taxation must be increased, a levy placed on taxi fares, and/or spending diverted from other areas. If additional revenues are raised, efficiency costs are involved. These should be taken into account when considering the benefits of deregulation and applying the public interest test. The Commission notes that in responding to the Freehills report, the ACT Government states that it considers that there is no statutory or other legal entitlement for compensation.

6.6 Matters considered by the Commission

The Commission is required to consider the 'degree of competition within the industry and the way in which that may affect the efficiency of the industry'. In assessing this issue, it is necessary to consider what barriers exist to competition, whether/how these impact on competition, and how these then flow through to efficiency consequences for the industry. What are the effects on the service providers, and similarly, how are consumers affected?

These issues have been considered widely within Australia over recent years. Reviews of the industry have been conducted at the national level¹⁵, and also by all state and territory governments.

Given the extent of work conducted recently, including the Freehills review of the ACT taxi and hire car industries, the Commission sees little value in reviewing afresh the competition and efficiency issues for the taxi industry. Instead, the Commission has considered the work that has been conducted recently in Australia.

Generally, these reviews reach similar conclusions. Key conclusions include:

- licence quotas have significantly restricted competition
- regulation imposes significant costs on consumers
- regulation has limited service innovation and the pursuit of cost efficiencies by operators in the taxi industry
- licence quotas/entry restrictions should be removed
- licence quotas are not essential to meeting safety concerns. Such concerns are best addressed directly through regulations supported by appropriate enforcement and sanctions.

On occasions, review conclusions differs in terms of how fares should be determined where entry restrictions have been removed. Differences have largely come about due to different market structures, eg dominance of phone bookings or rank and hail market. Issues also arise where cities have large airports. In such a situation, price haggling over fares would not allow the free flow of taxis and their passengers from the airport.

In some instances, where removal of entry restrictions has been recommended, a transitional approach has maintained maximum fare regulation. Once entry restrictions are removed, competition is likely to see some taxi operators offering fares lower than the regulated maximum. This has not generally occurred where licence quotas exist. Thus the regulated maximum fare has become the only fare.

¹⁵ Productivity Commission, *Regulation of the taxi industry*, Research paper, AusInfo, Canberra, 1999 and Industry Commission, *Urban transport*, Report no. 37, AGPS, Canberra, 1994.

However, any transitional approach to maximum fare regulation is a secondary issue compared to removal of licence quotas.

The key point of the above is that regulation of the taxi industry has significantly restricted competition. This has had flow on effects in terms of efficiency, and consumers have borne the costs associated with regulation. The Commission considers there are strong arguments to support the removal of competitive restrictions in the taxi industry, namely licence quota restrictions. In the context of the competition reviews, the NCCs assessment framework, and the ACT Government's response to the Freehills review, quota restrictions and other specific issues are considered below.

6.6.1 Licence quota restrictions

The ACT Government has stated it prefers a transitional approach to reform. It does not intend to release additional standard taxi licences, and proposes that a further review be conducted prior to June 2002. The scope of this review would include existing regulatory arrangements, community need and industry viability. Ten additional WAT licences have been released in response to the Freehills report.

The Commission is concerned that the identified benefits of taxi industry reform in the ACT, as specified in the Freehills report (with similar conclusions reached by other states and national reviews), may be delayed by the ACT Government's approach. The potential to meet national competition policy reform requirements is also of concern.

The Freehills report identifies significant efficiency losses associated with quota restrictions. Competition would remove these losses. It would also encourage taxi operators to minimise their costs (while meeting service level requirements), and provide a service level/price mix that consumers seek. The competitive barriers presented by quota restrictions limit competition in the industry, impact adversely on efficiency, with resultant net costs to the community. In responding to these findings, removal of quota restrictions is recommended in the Freehills report.

The NCC has stated that proposals for a transitional approach to reform must be accompanied by rigorous public interest justifications. Given the extensive resources that have gone into reviewing the taxi industry by state, territory and federal governments and the conclusions these reviews have reached, the Commission considers the public interest justification test a significant hurdle to achieve. The NCC is also concerned where recommended reform paths are not communicated. The ACT Government, following the Freehills recommendation to remove licence restrictions, is proposing a further review of the industry.

The NCC has stated that the ACT needs to make significant further reform progress in relation to taxi industry regulation. A failure to progress reform is likely to be regarded as a substantial failure to comply with national competition policy obligations. It is therefore likely that the ACT Government's transitional approach to taxi industry reform and the proposal for a further review of the industry will not meet the requirements of the NCC/national competition policy. This could impact on the level of national competition policy payments granted to the ACT Government.

To justify continued regulation (ie licence quota restrictions), the ACT Government would have to rigorously and clearly identify public interest justifications. The Commission recommends that such work be undertaken if quota restrictions are to remain in place. This would meet NCC requirements.

6.6.2 Wheelchair accessible taxis

The Freehills report recommends that the ACT Government retain the power to set minimum service standards for WATs which are equivalent to standard taxi service standards. The ACT Government has released an additional 10 WAT licences and intends to strengthen the enforcement of WAT licence requirements.

The Commission has considered this issue within the service quality chapter.

6.6.3 Fare regulation

Freehills recommends that until adequate new entry has occurred following removal of licence quotas, maximum fare regulation be maintained. The ACT Government has agreed with this, and proposed that the Commission maintain its role as fare regulator, and that operators continue to be allowed to charge below the maximum fare.

The Commission believes that adequate protection for consumers should be in place during any transition to a newly competitive environment. It therefore supports continued regulation of the maximum taxi fare. As discussed above, the current regulated environment has resulted in the maximum fare becoming the only fare. It is likely that removal of licence quota restrictions will encourage operators to offer fares below the regulated maximum.

However, the Commission notes that in a market where licence quota restrictions have been removed, particular care must be taken in applying a pricing methodology to set maximum fares. For example, under the new pricing approach which calculates a surplus/deficit figure, an increase in taxi numbers without an increase in demand would result in reduced average takings per taxi. In the pricing model, this would translate into a fare increase, other things being equal. This would be a perverse outcome, competition leading to fare increases. If quota restrictions were removed and maximum fare regulation maintained (at least initially), the Commission would be careful to avoid any inappropriate pricing outcomes.

Freehills also recommends that if maximum fare setting regulation is maintained, consideration should be given to additional factors in the methodology, including factors to account for benchmarking or change of interstate prices, technology, productivity, cost of capital, driver earnings and/or demand elasticities.

The Commission's development of a new pricing approach has addressed many of the issues raised by Freehills. For example, the issue of driver earnings has been accounted for, and there is some comparison of inputs to the model with operations in other states. This allows a 'reasonableness' check to be done on the inputs. However, at this stage, the Commission does not see value in undertaking an extensive benchmarking exercise with interstate operators. The requirement for such work in the future will depend on the regulatory approach adopted by the ACT Government. Under the national competition policy reform agenda, a final decision on reform of the industry is required by 30 June 2002.

6.6.4 Taxi networks

Freehills recommends that consideration be given to establishing an additional network operator in the ACT to compete with the existing network provider, Aerial Taxi Cabs Co-operative Society Limited/Canberra Cabs. It also recommends that for the new non dominant network, minimum response time standards be removed or reduced sufficiently to permit new entry at the network level.

In response, the ACT Government has stated that until network accreditation arrangements have been settled, the introduction of an additional network will be invited on similar terms and conditions to those applying in the Government's agreement with Canberra Cabs. The ACT Government has recently called for tenders for the provision of a taxi network service.

The Commission generally supports the introduction of an additional network provider for the ACT. The benefits of competition at the network level should be pursued along with competition at the taxi operator level. Competition efficiencies generated at the network level should imply additional efficiencies at the taxi operator level. In a suitably competitive environment, these efficiencies would be shared with customers through lower average fares.

However, the Commission has some minor concerns with the ACT Government's proposal. Supply of network services may exhibit economies of scale. That is, the average cost of providing the service falls as production increases. In terms of network operators, the cost of their services may be expected to fall as the number of taxis served increases, ie the cost of the network service is spread over a greater number of taxis.

Canberra Cabs has argued that an additional network is not feasible in the ACT, and network competition may lead to an operator established in another capital city becoming the network operator for the ACT. That is, competition may lead to the existing Canberra Cabs network no longer serving the ACT taxi industry.¹⁶ It is difficult to assess the likelihood of such a scenario.

The Commission generally supports the ACT Government's proposal to increase competition, and notes that further regulatory reform (ie removal of quota restrictions) may have the effect of:

- increasing the number of taxis in the ACT
- increasing the level of competition between taxi operators
- developing innovative taxi services
- increasing demand for taxi services.

Each of the above would act to support multiple network operators in the ACT.

The full benefits of reform are unlikely to be achieved via a piecemeal approach. Thus, the full benefits of an additional network operator will not be realised in an environment where licence quota restrictions exist. The Commission's comments on licence quota restrictions are contained in section 6.6.1 above. Further, the Commission would be concerned if a new

¹⁶ Canberra Taxi Proprietors Association and Canberra Cabs, *Submission to determination of prices for taxi services review*, January 2001, p 3.

network operator was not given adequate opportunity to meet service requirements. During the initial period of its operation, the Commission would encourage the ACT Government to consider the network's performance in the context of supporting the establishment of an additional network operator (the Commission notes above that such an approach seems to have been taken with the incumbent network operator, where service requirements have not been achieved and other aspects of the MoU have not been enforced) – see service quality chapter.

The Commission is not suggesting that service standards be allowed to fall. Rather, that any new operator have an adequate opportunity to meet the service standard requirements.

6.6.5 Cross border restrictions

Freehills recommends that the ACT Government work with its NSW counterpart to establish a single taxi regulatory regime for the ACT/Queanbeyan region. The ACT Government has entered into discussions with the NSW Department of Transport.

Notwithstanding the wider issues that must be resolved in establishing a single market, the Commission supports this development. It has the potential to increase competition at the network provider level, as well as the taxi operator level. Customers should benefit through the creation of the single market.

7 OTHER ISSUES

7.1 Financial viability

Under section 20 of the *Independent Pricing and Regulatory Commission Act 1997*, the Commission is to consider financial viability factors:

- an appropriate rate of return on any investment in the regulated industry - section 20(2)(d)
- 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 - section 20(2)(i).

The existing taxi cost index does not require consideration of an appropriate rate of return for the industry. Rather, the index concentrates on operating costs and return of capital as factors underpinning determination of fare levels. The Commission's initial review of taxi fares finds that disadvantages of this approach include:¹⁷

- preventing the pricing regulator from being able to properly assess the impact of price decisions on the financial viability of persons providing taxi services
- 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 pricing regulator to adjust prices in accordance with the returns available from competing investment opportunities in the economy.

In chapters 3 and 4, the Commission has considered options for including a rate of return and corresponding capital base in the fare setting methodology. As these discussions indicate, a range of issues must be considered in applying such a methodology. Key among these is the plate values to be included in the calculations, and determination of an appropriate rate of return.

Given the trading of taxi licences, owners would have paid varying amounts for their taxi plates. At issue is the appropriate figure to use if plate values/rate of return are to be included in the fare setting methodology. The Commission notes that in other industries (eg electricity, gas), there has been considerable debate regarding whether appropriate financial returns should be assessed against historical cost of the initial investment, or some current cost equivalent.

The borrowing, capital and cash flow requirements of a taxi operator closely relate to the costs of providing the taxi service. These cost issues have been closely considered by the Commission in developing the new fare setting methodology - see chapter 3 'industry costs and efficiencies'.

The Commission invites submissions on these issues.

¹⁷ ICRC, *Taxi fares for 2000-2001*, Final price direction, June 2000, p 21.

7.2 Environmental factors

Under section 20 of the *Independent Pricing and Regulatory Commission Act 1997*, the Commission is to consider environmental factors:

- 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 – section 20(2)(f)
- considerations of demand management and least cost planning – section 20(2)(h).

Public transport provides an alternative to the use of private motor vehicles. The benefits of public transport include reduced congestion and pollution. The extent to which these benefits can be realised will depend on factors such as the relative cost of public versus private transport options and the propensity for private vehicle users to switch to public transport. This, in turn, will be influenced by accessibility, service quality and frequency of public transport.

Traditionally, the above factors have been discussed in respect of public transport options such as rail and buses. Those forms of mass transit provide the greatest opportunity to reduce congestion and pollution. Nonetheless, taxis do provide an alternative form of public transport, and an environmentally superior alternative to greater use of private motor vehicles.

In its first determination of maximum taxi fares in the ACT, the Commission allowed fares for the 12 month period from 1 July 2000 to incorporate:

- a 7.71 per cent increase in average taxi charges based on cost increases over the previous 12 months
- a net 7.85 per cent GST adjustment after allowing for cost savings from the Federal Government's 'A New Tax System' package.

The Commission noted that although taxi fares would increase in real terms, it was important to consider the likely diversion of passenger journeys from taxis to private motor vehicles. The Commission concluded that given the varied factors that contributed to choice of transport mode, there would not be a significant increase in environmental or air quality problems.¹⁸

The Commission is now proposing that there be no fare change from 1 July 2001. Obviously, this will have no adverse effects on taxi patronage.

Canberra Cabs has indicated that greatest demand for taxi services comes from business users. Generally, this is associated with weekday demand peaks occurring in the morning and late afternoon. Relatively high demand also takes place during Friday and Saturday nights, and early Saturday and Sunday mornings. Price rises are unlikely to have a significant effect on taxi use by these groups. Other factors apart from fare levels will influence business and social users of taxis.

¹⁸ ICRC, *Taxi fares for 2000-2001*, Final price direction, June 2000, p 24.

The Commission observes that over recent years, taxi patronage has fallen slightly overall. The design of Canberra and Canberrans attachment to private vehicles suggests that, other things being equal, patronage may only ever grow slowly. However, the removal of licence quota restrictions, and the potential for competition to lead to innovative services and new service level/price combinations, may encourage some additional growth in taxi patronage.

The Commission has considered environmental factors in making its draft decision, and believes that the maintenance of existing fares would encourage greater use of taxi services.

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 2001 addressing the following:

1. the methodology which will be used 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; and
2. the recommended maximum fares for the regulated taxi services for a period of two years from 1 July 2001.

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.

If appropriate the Commission may wish to firstly examine and report on the methodology which will be used to determine fares for taxi services and then having completed that review recommended maximum fares for the regulated services.

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 2001 to 30 June 2003 is to be provided to the Minister for Urban Services by 30 May 2001;

Dated this 6th day of November 2000

BRENDAN SMYTH
MINISTER FOR URBAN SERVICES

ATTACHMENT 2 CANBERRA CABS SUBMISSION

The Canberra Taxi Proprietors Association and Canberra Cabs (together referred to as Canberra Cabs) submission proposes a 7.8 per cent increase to taxi fares from 1 July 2001, with an automatic adjustment after 12 months. The submission also highlights key issues for the industry. These key issues are summarised below.

Competition within the ACT taxi industry

The Canberra Cabs submission notes the future increase in the number of taxis in the ACT. There is the potential for an additional 26 taxis to operate in the ACT in 2001, an increase of 11 per cent on the current fleet. This compares to reduced demand over 1995 - 2000, and will significantly increase competition in the supply of taxi services.

The effect of increased taxi numbers and reduced demand will see average hirings per taxi fall, producing significantly adverse effects on the income potential for each taxi.

Canberra Cabs also notes the ACT Government's call for tenders to establish a second taxi network in the ACT. The submission states that the ACT market size (population of 310,000) is only sufficient for one network operator, and that this is supported by comparisons to other capital cities. For example, in Brisbane there are two networks serving 863,769 people.

The submission states that if an additional network operating out of Sydney (or another capital city) were allowed to operate in the ACT, then the size of its existing network would allow it to charge lower fees and there would be the real possibility that the ACT could end up with one network operating out of another capital city. This would have employment and economic consequences for the ACT.

Measures of Efficiency

The Dispatch Service

The technology used in the ACT for data dispatch is identical to that used in other capital cities in Australia, but in Canberra the cost is recouped from a much smaller base. Canberra Cabs' base fees are recouped from 233 taxis and are therefore higher than the base fees on a network in Sydney with approximately 3,500 taxis to spread its costs. The consumer in the ACT, has benefited from the introduction of technology by experiencing the efficiency and safety that technology brings but without a flow-on of the full cost. The full cost of technology has not been passed on to the consumer.

The Customer

Accreditation benchmarks have been met by Canberra Cabs' network for each reporting period since the introduction of accreditation in 1997. Only since the introduction of an additional 10 WAT licences, have the response times for WAT hirings been below the benchmark.

Quality of Vehicles

Inspections are conducted quarterly, concentrating on the vehicle and driver presentation, and is strictly enforced. Cars not meeting the required standard are given on the spot written notices of the defect, with a time/date by which the defect is to be repaired. Any defect associated with safety requires an immediate response, while operators may be given two weeks to have minor defects corrected.

Change-Over Times

In the ACT, as a sole network provider, Canberra Cabs has introduced a By-Law which prohibits taxis from changing over during the peak period (3:00 - 5:00pm on week days) allowing flexibility for changeover before 3:00pm or after 5:00pm, and for this to be varied from day to day to accommodate different drivers commitments. This has increased the availability of the taxi resource by 20 per cent during this period and can be monitored by a single network.

The role of the GPS

Canberra Cabs has recently upgraded its data dispatch network to include the most advanced capabilities associated with global positioning system (GPS) dispatch, but is restricted in its capacity to deliver efficiencies.

The system presently being investigated by Canberra Cabs, and within the capability of Canberra Cabs' new software, is a GPS/zone queuing variable system. Ideally, a taxi will be monitored at frequent intervals (seconds) for its GPS location, and depending on the zone in which the hiring is located, will determine the weighting given to GPS/zone queuing preference. This will allow the computer to identify a number of cars within a certain radius of the hiring by their GPS location, but to then allocate the hiring to the vehicle within that radius, which has been vacant the longest.

Dead Running

Data dispatch introduced efficiencies in that drivers could interrogate the computer and pre-position themselves for a hiring. Often, this means driving considerably more dead kilometres. Consumers benefit because the taxi has been pre-positioned and is available with shorter response times for the hiring. While taxi fares may not fall, consumers benefit from a better response time.

Recommendation for maximum fares

The Terms of Reference requires the Commission to recommend maximum fares for the regulated taxi services for a period of two years.

Canberra Cabs are strongly of the opinion that the Commission should determine a fare increase to commence on 1 July 2001, with an automatic adjustment after twelve months. Annexure A to their submission calculates a fare increase of 7.81 per cent. Two options have been presented for the application of the fare increase and it is strongly recommended that Option 2 be adopted. Option 2 lessens the impact of the increase on flag fall and more closely aligns the ACT with other states.

Because of the considerable uncertainty surrounding the ACT Taxi Industry in the next one to two years, it is recommended that the Commission accepts an automatic adjustment to fares at the end of twelve months, based on the application of March 2002 costs to the price index. The grounds for this recommendation are that there have always been significant adjustments to costs over which the industry has no control.

Following is Canberra Cabs' calculation of the 7.81 per cent increase to fares:

**2001
TAXI INDUSTRY
PRICE INDEX
COMPARATIVE TABLE**

ITEM	2000 ACTUAL COSTS	2000 ICRC COSTS	2001 ACTUAL COSTS	% CHANGE FROM 2000 ACTUAL COSTS	% CHANGE FROM 2000 ICRC COSTS
1. FIXED COSTS					
1.1 Depreciation	6811	6231	7029	3.20	12.81
1.2 Registration costs	5804	5754	6757	16.41	17.43
1.3 Driver's licence	22	22	22	0.00	0.00
1.4 Comprehensive insurance	6653	6586	7832	17.72	18.91
1.5 Illness and accident insurance	1432	1418	1881	31.35	32.65
1.6 Workers' compensation insurance	843	835	1737	106.04	108.02
1.7 Superannuation	3755	3755	4385	16.77	16.77
1.8 Base fees	11076	10987	11854	7.02	7.89
1.9 Safety camera	<u>0</u>	<u>0</u>	<u>600</u>	<u>N/A</u>	<u>N/A</u>
Sub total	36396	35588	42097	15.66	18.28
2. VARIABLE COSTS (NON-LABOUR)					
2.1 Fuel	16524	16111	18936	14.59	17.53
2.2 Tyres	1800	1494	1600	-11.11	7.09
2.3 Repairs and Maintenance	15324	13605	14870	-2.96	9.29
2.4 Miscellaneous	<u>2681</u>	<u>2654</u>	<u>2703</u>	<u>0.80</u>	<u>1.84</u>
Sub total	36329	33864	38109	5.34	15.96
3. VARIABLE COSTS (LABOUR)					
3.1 Labour	<u>94600</u>	<u>94600</u>	<u>96670</u>	<u>2.18</u>	<u>2.18</u>
Sub total	94600	94600	96670	2.18	2.18
TOTAL COST	167325	164052	176876	5.70	7.81

ATTACHMENT 3 APPRAISAL OF EXISTING COST INDEX

The appraisal focuses on the extent to which the existing taxi cost index is a reasonable reflection of current operations and costs in the ACT taxi industry. In this regard, it should be noted that, from its inception, the cost index was not designed to reflect industry costs in an absolute sense and therefore to use for setting absolute fares; but rather to provide a reasonable basis for adjustments of fares to reflect cost escalation. However, it might be commented that a model which does not reasonably reflect absolute costs is unlikely to reasonably reflect changes in costs over time.

The Commission's appraisal is based heavily on:

- the Canberra Cabs submission in response to the Commission's Issues Paper: Determination of Prices for Taxi Services
- information provided at a meeting between Canberra Cabs and the Commission (16 February 2001).

Detailed Appraisal

The Commission's detailed item-by-item appraisal of the current cost index, is given in the table below. For each cost item this gives:

- basis of costing
- price sources
- relevant costs as at January 2001
- critique and comments.

All except this last column are based heavily on the Canberra Cabs submission.

Main Findings

The current cost index provides a set of costs relating to the ownership and typical operation of a single taxi for a year. It is not directly concerned with taxi earnings.

The following summarises the main cost areas in which we consider that the current cost index is significantly deficient as reflecting current typical taxi industry costs in ACT:

1. vehicle capital (item 1)
 - current costs over-estimate average vehicle depreciation because they are based exclusively on the costs of new vehicles with a functional life of four years. They do not allow for the mix of new and second-hand vehicles in the fleet and the range of years for which each are used. A more reasonable working assumption would be to assume that 50 per cent of the fleet was new vehicles, which are sold after five years, and the remaining 50 per cent are on average three years old at purchase and are sold after a further four years
 - current costs are understated to the extent that they ignore any interest charges on vehicle capital (these are real financial costs, as most owners lease vehicles).

2. fuel (item 10)
 - costs are based on an average vehicle travelling 180,000 km per annum, whereas the current ‘typical’ estimate is 206,000 km per annum. A Canberra Cabs’ survey figure gave an average of 190,400 km. However, Canberra Cabs advise that they do not place a high reliance on that survey figure, and that 206,000 km is a more accurate reflection of actual distance travelled
 - costs are based on LPG consumption of 5.0 km per litre, whereas the current ‘typical’ estimate is 5.5 km per litre. Canberra Cabs agree that this is a reasonable estimate.
3. hirings per car
 - Canberra Cabs indicates in its submission (page 3) that average hirings per car in 2000 amounted to 11,708. This represents a 6 per cent reduction on the corresponding 1999 figure. The Commission has some concerns with this figure. Close analysis of demand figures for 1999 and 2000 indicate that the fall in demand in 2000 was concentrated in the second half of the year. Comparison of first half demand for 1999 and 2000 indicates that total demand grew by around 2 per cent, and telephone bookings by 3.3 per cent.

There is the strong likelihood that the fall in demand in the second half of 2000 was associated with reduced business activity during the Sydney Olympic Games. Discussions with Canberra Cabs indicate that the business market is a key driver of taxi demand in the ACT. This market reduced significantly in the second half of 2000. The Commission considers it appropriate to adjust demand for the effect of the Olympics. A more reasonable annual estimate is assumed to be 12,145, which represents a 2.5 per cent reduction on the 1999 figure. Given the relatively high number of average kilometres adopted in the model (206,000), it has been assumed that the increase in average hirings has been accompanied by a corresponding reduction in dead kilometres.
4. tyres, repairs and maintenance (items 11, 12)
 - as with fuel, costs are based on 180,000 km per annum, whereas the current typical estimate is 206,000 km per annum.
5. driver labour (item 14)
 - costs (including superannuation and workers compensation) are \$30,000 - \$35,000 per annum too high relative to actual earnings achieved by ACT taxi drivers
 - this item is the largest single contributor to the cost index, representing 55 per cent of total costs. Consequently, it has by far the greatest (absolute) divergence from actual earnings by taxi drivers, with the divergence accounting for 15 - 20 per cent of total costs.

In addition to the above, the Commission notes that the existing cost index includes no allowance for the opportunity cost/interest charge relating to the cost of taxi plates. Whether and how the opportunity cost of plates should be included in a model designed for taxi fare-setting is discussed in the report.

ACT TAXI COST MODEL: BASIS, COST INPUTS AND CRITIQUE						
Item	Basis	Price Sources ⁽⁵⁾	Costs at January 2001			Critique/Comments
			Total (\$)	Annual (\$)	Per km (¢)	
OPERATIONS ASSUMPTIONS	<ul style="list-style-type: none"> operations and costs of single vehicle owner-driver and 1 bailee driver 120 hours operation/week, 50 weeks pa 180,000 total kilometres pa. 					Does not reflect current typical operation/vehicle. Typical figures now 143 hours/week for 50 weeks, 206,000 kms pa.
1. Vehicle Depreciation	Depreciation assumes a functional life of 4 years for the basic vehicle, gas conversion equipment and meter. It is based on purchase of new vehicle, sale after 4 years.					<p>Assumes new vehicle sold after 4 years, which will over-estimate average depreciation. More reasonable assumption for average might be 50% of vehicles purchased new, sold after 5 years; 50% purchased age 3 years, sold after 4 years.</p> <p>No allowance made for interest payments/opportunity cost of capital. In practice, most vehicles purchased on lease (new 4-5 years, s/hand 3-4 years), with 10% residual.</p>
1.1 Value of vehicle	Current model Ford Falcon sedan with power steering, automatic transmission, air conditioning and bucket seats (registration and insurance not included).	1	31,290			
1.2 Gas conversion	Supply and fit dual fuel gas conversion: average of Impco type (\$2136), Vialle type (\$2309).	9	2,223			
1.3 In-car electronics	Remove and install Motorola radio equipment (\$200), EFTPOS equipment (\$70) and GPS equipment (\$60).	10	330			
1.4 Meter	Supply and fit Schmidt meter.	10	531			
1.5 Residual value (income)	Sale of 4 year old vehicle, including gas equipment, for 20% of purchase price	1,9	(6,258)			
	Sub-total (net)		28,116	7,029		
2. Registration Costs						
2.1 Gas leak certificate		9		25		-
2.2 Registration fees		2		332		-
2.3 Third party personal insurance		2		5,904		-

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ACT TAXI COST MODEL: BASIS, COST INPUTS AND CRITIQUE																		
Item	Basis	Price Sources ⁽⁵⁾	Costs at January 2001			Critique/Comments												
			Total (\$)	Annual (\$)	Per km (¢)													
2.4 Taxi operator's licence		2		<u>496</u>														
	Sub-total			6,757		-												
3. Driver's Licence	\$111 for 5 year licence	2		22		-												
4. Comprehensive Insurance																		
4.1 Vehicle comprehensive insurance.	Based on new vehicle value of \$31290 exclusive of gas, radio, EFTPOS and GPS equipment and meter. Allows for average vehicle value as 65% of new value.	14		6,232		Figure calculated as follows: <ul style="list-style-type: none"> • full quoted cost of CI on new vehicles is \$10,388 (including TPPI component of \$1,600). • GST component of this is \$799, giving a remaining amount of \$9,589 (GST is retained on the TPPI portion, as no ITC applies). • take 65% of this to allow depreciation, giving \$6,232. Resulting figure may be too high as vehicle values do not recognise proportion of older (s/hand) taxis in fleet. Also rate does not allow for no-claims bonus. Standard value (including GST as no ITC applies). This amount is double-counted with Comp Insurance (above): this error is long-standing and has not been corrected, in order to ensure consistency.												
4.2 Third party property insurance		14		<u>1,600</u>														
				7,832														
5. Illness and Accident Insurance	Illness and accident insurance providing for income maintenance of \$24100 per year (75% of net income of \$32134 per year), owner/driver, male smoker, subject to qualifying period of 14 continuous days; for a monthly benefit of \$2008 (Note 3). Age Annual Stepped Premium (Benf for 2 years) (Benfs to age 65)	4,5		1,881		Net income figure of \$32,134 pa was originally derived as an 'agreed' estimate, adjusted over time by movement in an appropriate index (AWE).												
	<table border="0"> <tr> <td>30</td> <td>\$926</td> <td>\$1,156</td> </tr> <tr> <td>40</td> <td>\$1,226</td> <td>\$2,274</td> </tr> <tr> <td>50</td> <td><u>\$2,164</u></td> <td><u>\$3,540</u></td> </tr> <tr> <td>Totals</td> <td>\$4,316</td> <td>\$6,970</td> </tr> </table> Average = \$1,881	30	\$926	\$1,156	40	\$1,226	\$2,274	50	<u>\$2,164</u>	<u>\$3,540</u>	Totals	\$4,316	\$6,970					
30	\$926	\$1,156																
40	\$1,226	\$2,274																
50	<u>\$2,164</u>	<u>\$3,540</u>																
Totals	\$4,316	\$6,970																

ACT TAXI COST MODEL: BASIS, COST INPUTS AND CRITIQUE						
Item	Basis	Price Sources ⁽⁵⁾	Costs at January 2001			Critique/Comments
			Total (\$)	Annual (\$)	Per km (¢)	
6. Workers Compensation Insurance	Workers comp insurance for ACT for retained earnings of \$47,966 based on 60 hours per week, 52 weeks per year for one driver (calculated in accordance with item 14), including \$59 broker's fee.	4		1,737		\$47,996 figure based on 70 paid hours per week (40 base hours, 20 overtime hours at 1.5 rate) at \$527.10/40 hours for 52 weeks (item 14). (No WC payment on holiday loading.) Need to pro-rate if adjust driver labour (item 14).
7. Superannuation	Superannuation payment based on 8% of labour (cost (item 14) for earnings for 40 hours per week over 12 months for 2 drivers.	6		4,385		OK, assuming driver labour OK (item 14). Need to consider along with driver labour and to adjust if adjust driver labour.
8. Base Fees		3		11,854		Represents standard fees per vehicle for calendar year 2001. Base fees were approximately doubled in 1998 (following introduction of the computer dispatch system). However this one off adjustment was not covered by a fare increase, and Canberra Cabs notes that "only increases since 1998 have been addressed in fares". (In the 1998 fare determination, the Base Fees for 1997 were adjusted from the corresponding figure used for the 1997 determination; but with a zero increase in fees 1997-98 for fare purposes.) Note that, as the existing model includes the full base fees, the weighting of the base fees in the model approximately doubled from 1998.
9. Safety Camera	Lease of safety camera @ \$50/month	3		600		-
10. Fuel	180,000 kms pa (120 hours/week for 50 weeks at 30 km/hr). Consumption 5.0 kms/litre Price 52.6¢/litre (as at 31 Jan 01).	7		18,936	10.52	Typical operation now increased to 206,000 km pa. Typical consumption now estimated at 5.5 kms/litre.

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ACT TAXI COST MODEL: BASIS, COST INPUTS AND CRITIQUE						
Item	Basis	Price Sources ⁽⁵⁾	Costs at January 2001			Critique/Comments
			Total (\$)	Annual (\$)	Per km (¢)	
11. Tyres	Supply of 4 sets of tyres based on annual travel of 180,000 kms and consumption rate of 45,000 kms per set. Type - cost per tyre Dunlop Monza 65/15/205 \$104.50 Dunlop Monza D8 65/15/205 <u>\$95.50</u> Average \$100.00 Annual cost = 4 x 4 x \$100	8		1,600	0.89	Typical operation now increased to 206,000 kms pa (above) cost rate (0.89¢/km) very comparable with interstate data.
12. Repairs and Maintenance	Figures based on 180,000 kms pa.					Typical operation now increased to 206,000 kms pa (above). Overall cost rate (8.26¢/km) very comparable with interstate data.
12.1 General R&M	Supply repairs and maintenance as described in the Repairs and Maintenance schedule (CC Submission Annex A p5).	1		12,724		
12.2 Gas conversion	Supply and fit gas converter overhaul kit once per year for: Impco (\$236), Vialle (\$332). Average = \$284.	9		284		
12.3 Motor R&M	Repair of Schmidt meter once per year (\$90) and fare rate adjustment, including recalibration (\$100).	10		190		
12.4 Miscellaneous electrical	(Note 1)	N/A		283		
12.5 Miscellaneous mechanical repairs.	(Note 1)	N/A		<u>1,389</u>		
				14,870	8.26	
13. Miscellaneous						
13.1 NRMA membership		15		46		
13.2 Car washing	1 major wash (\$15.45) plus 3 minor washes (\$6.90) per week.	12, 13		1,879		Plausible

ACT TAXI COST MODEL: BASIS, COST INPUTS AND CRITIQUE						
Item	Basis	Price Sources ⁽⁵⁾	Costs at January 2001			Critique/Comments
			Total (\$)	Annual (\$)	Per km (¢)	
13.3 Admin costs (non-labour)	Various costs associated with telephone, bank, accountant, maintenance of commercial accounts, car accessories and maps etc. (Note 2)	N/A		778		Plausible. No allowance for admin labour costs appears to be included in the model. Note previous figure adjusted for only 9 months inflation.
14. Driver Labour	Based on: <ul style="list-style-type: none"> 120 hours/week: 2 drivers, 80 hours normal time, 40 hours 1.5 times ordinary earnings rate per driver of \$527.10/40 hour week (52 weeks pa) plus 17.5% holiday loading on 4 weeks pa. rate originally based on Comcar driver award, subsequently adjusted using changes in ACT AWE (ordinary time earnings, full-time adults). 	11		96,670		Not reflective of actual earnings by taxi drivers. Canberra Cabs figures based on model in IPART review give gross takings of \$163,493 pa for 7,150 driver hours, equating to \$22.87/hour. Bailee drivers get paid 50% of this, giving a rate of \$11.43/hour. For 6000 hours pa (in this Model), this gives \$68,580 pa. This also has to cover driver superannuation (item 7). Alternative (approximate) approach is to take driver labour as 50% of total costs, ie. equal to all other costs (excl driver superannuation). This gives figure of approx \$75,800 (incl superannuation). Note previous figures adjusted for only 9 months inflation.
GRAND TOTAL				176,876		

Notes:

- Miscellaneous auto electrical and mechanical repairs are adjusted on the difference between the cost of item 12.1 over the current and previous period, which decreased by 3.12%
- Item 13.3 are adjusted on movements in the Canberra All Groups CPI, which increased by 5.65% (from 123.7 to 130.7) over the 9 month period from December 1999 to September 2000.
- Figure for net income is adjusted on movements in the Canberra All Groups CPI, which increased by 5.65% (from 123.7 to 130.7), over the 9 month period from December 1999 to September 2000.
- Item 14 is adjusted on movements in Average Weekly Earnings, Full-time Adults, Ordinary Time Earnings - ACT (original series), which increased by 2.19% (from 897.60 to 913.70) over the 9 month period from November 1999 to August 2000.
- Refer to Canberra Cabs Submission for details.

ATTACHMENT 4 NEW COST AND PRICING MODEL

Having considered alternative model formulations, the preferred model approach is similar to the model put forward by one of the NSW taxi companies to the IPART review of the NSW taxi industry (although not in the context of fare setting). The Commission has made some minor adjustments to the structure of this model, and modified it to incorporate operations and costs typical of the ACT taxi industry.

The operations and cost inputs to the model are based on those provided by Canberra Cabs, but with some modifications in cost items to better reflect typical cost levels. These modifications have been determined following points discussed at a meeting with Canberra Cabs on 16 February 2001.

The model essentially provides a profit and loss statement for a typical taxi operation in the ACT, from the perspective of the vehicle owner. It relates to a single vehicle, operating for 206,000 km (7,150 driver hours) per year. Two sub-models have been developed: one assuming the owner drives (55 hours/week) and also sub-contracts to bailee drivers (88 hours/week); the other that bailee drivers cover all hours.

For each sub-model a gross surplus to the owner is derived (before any return on either his/her labour or the value of taxi plates); we can then consider what would be reasonable returns on these two items and examine the effects of these assumptions on the 'net' surplus.

A summary of model results (based on current fares and January 2001 operating expenses) is given in the table below, and a detailed derivation of each cost item follows this.

The key finding is that, after allowing a reasonable return on owner-driver labour (equal to the hourly rate earned by bailee drivers), the owner surplus is about \$10,600 - \$12,700 pa (in both sub-models). This represents a 6 - 7 per cent margin on total revenues.

If the opportunity cost of plates were to be ignored, this indicates that a zero surplus could be obtained if fare revenues were reduced by \$21,200 - \$25,400 pa (some 12 - 14 per cent) - assuming bailee driver payments reduced pro rata (under the way bailee drivers are paid, the net effect on the owner surplus is half the change in gross revenues).

PROPOSED ACT TAXI PROFIT & LOSS/PRICING MODEL – SUMMARY⁽¹⁾		
Item	Annual Cost (@ January 2001)	
	Owner-driver + bailee drivers	Bailee drivers only
REVENUES		
Gross takings	169,595	169,595
Non-fare income	3,895	3,895
Total Revenue	173,490	173,490
OPERATING EXPENSES		
Fixed Costs		
1. Vehicle capital costs	5,354	5,354
2. Vehicle registration costs	6,757	6,757
3. Driver licence & medical	61	-
4. Safety camera	600	600
5. Comprehensive insurance	4,410	4,410
6. Network fees	11,854	11,854
7. Office/miscellaneous expenses	2,205	2,205
Sub total	31,241	31,180
Variable Costs: Non-labour		
9. Fuel	19,700	19,700
10. Tyres	1,831	1,831
11. Car washing	1,136	1,136
12. Repairs and maintenance	17,282	17,282
Sub total	39,949	39,949
Variable Costs: Driver labour		
Driver payments (bailee drivers)	52,183	84,797
Administration labour (bailee drivers)	1,225	1,838
13. Workers compensation insurance (bailee drivers)	1,884	3,027
8. Illness/accident insurance (owner-driver)	2,028	-
Sub total	57,320	89,662
Total Operating Expenses	128,510	160,791
Gross Surplus (Rev-Op Exp)	44,980	12,699
Return on owner-driver labour ⁽²⁾	34,391	-
Net surplus (after return on labour)	10,589	12,699

Notes:

1. Detailed basis given in table below.
2. Based on 58 hours/week (including 3 hours administration), 50 weeks pa, \$23.718/2 per hour (ie. same rate as earned by bailee drivers).

PROPOSED ACT TAXI PROFIT & LOSS/PRICING MODEL				
Item	Basis/Notes	Amounts @ January 01		
		Total - \$ pa.		Per km - ¢/km
		Owner-driver + bailee drivers	Bailee drivers only	
OPERATIONS ASSUMPTIONS	<ul style="list-style-type: none"> operations of single vehicle operated by either owner-driver and bailee drivers; or all bailee drivers. operates 143 hours/week (13 shifts * 11 hours), 50 weeks pa = 7,150 hours pa (owner-driver does 55 hours/week). 206,000 total kms pa (50% in revenue service). 			
REVENUES (at current fares)				
Gross takings.	Canberra Cabs best estimate of gross takings/car, based on: <ul style="list-style-type: none"> 12,145 average hirings/car average fare/hiring (\$13.964), based on 8.8 kms distance, waiting time 1 minute, radio fees, mean of Tariff 1 and Tariff 2 rates. (Equates to \$23.718/driver hour). 	169,595	169,595	
Other (non-fares) Income.	Canberra Cabs estimate of average Trading and Investment Rebates available to Canberra Cabs members.	3,895	3,895	
Total Revenues		173,490	173,490	
EXPENSES (Jan 2001 rates)				
A. FIXED COSTS				
1. Vehicle Capital	Assume 50% vehicles purchased new, retained 5 years; 50% purchased 3 years old, retained 4 years. <ul style="list-style-type: none"> vehicle values depreciated 33.1% pa dv basis (equivalent to 20% of original value after 4 years). new vehicles cost \$31,290 (residual value \$4,185 after 5 years); extras \$3,084 (zero residual).second-hand vehicles cost \$9,358 (allowing 3 years depreciation), residual value \$1,872 age 7 years; extras as for new vehicles. average annual costs calculated (mortgage basis) at 7.5% pa real interest rate (consistent with typical finance lease rates). 	5,354	5,354	
2. Vehicle Registration Costs	As per existing cost index	6,757	6,757	
3. Driver Licence & Medical				
3.1 Driver Licence	<ul style="list-style-type: none"> \$111 pa for 5 years, owner-driver only. 	22		
3.2 Medical Examination	<ul style="list-style-type: none"> Owner-driver only. 	39	-	
		61		

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PROPOSED ACT TAXI PROFIT & LOSS/PRICING MODEL				
Item	Basis/Notes	Amounts @ January 01		
		Total - \$ pa.		Per km - ¢/km
		Owner-driver + bailee drivers	Bailee drivers only	
4. Safety Camera	Lease at \$50/month.	600	600	
5. Comprehensive Insurance				
5.1 Taxi Comprehensive Insurance	<ul style="list-style-type: none"> vehicle values as per item 1 (average start year value 35.2% of new value). rate 25.53% of vehicle value at start of year (as per Canberra Cabs). 	2,810	2,810	
5.2 Third Party Property Insurance	<ul style="list-style-type: none"> standard rates (as Canberra Cabs). 	1,600	1,600	
		4,410	4,410	
6. Network Fees	Standard Canberra Cabs rate per vehicle, calendar year 2001.	11,854	11,854	
7. Office/Miscellaneous Expenses				
7.1 Office expenses: non-labour	<ul style="list-style-type: none"> as per Canberra Cabs. 	2,159	2,159	
7.2 NRMA membership	<ul style="list-style-type: none"> as per Canberra Cabs. 	46	46	
		2,205+	2,205+	
B. VARIABLE COSTS: NON-LABOUR				
9. Fuel	<ul style="list-style-type: none"> as per Canberra Cabs - 206,000 kms pa, 5.5 kms/litre, 52.6¢/litre. Canberra Cabs note that consumption rate is a reasonable estimate, but not supported by survey information. This rate sensibly consistent with interstate evidence. 	19,700	19,700	9.56
10. Tyres	<ul style="list-style-type: none"> as per Canberra Cabs - 206,000 kms pa, 45,000kms/tyre, \$100/tyre. 	1,831	1,831	0.89
11. Car Washing	<ul style="list-style-type: none"> as per Canberra Cabs - \$21.85/week * 52 weeks. 	1,136	1,136	0.55
12. Repairs & Maintenance	<ul style="list-style-type: none"> as per Canberra Cabs. 	17,282	17,282	8.39
C. VARIABLE COSTS: DRIVER LABOUR				
Driver Payments	<ul style="list-style-type: none"> 50% of takings for bailee drivers takings \$23.718/driver hour (refer Revenue) bailee driver hours 88 or 143/week (refer Operations). has to cover any superannuation payments. 	52,183	84,797	

PROPOSED ACT TAXI PROFIT & LOSS/PRICING MODEL				
Item	Basis/Notes	Amounts @ January 01		
		Total - \$ pa.		Per km - ¢/km
		Owner-driver + bailee drivers	Bailee drivers only	
Administration Labour	<ul style="list-style-type: none"> based on CC 'reasonable estimates': approx 51.65 hours pa per bailee driver, at driver rate of \$23.718/2 per hour. (Estimates also allow c.3 hours/week for owner-driver administration.) no survey evidence available on administrative time, but estimates appear plausible. 	1,225	1,838	
13. Workers Compensation Insurance	<ul style="list-style-type: none"> workers comp on earnings of bailee drivers (as above). as per Canberra Cabs, but adjusted for higher revenue and hence earnings figures (+3.73%). 	1,884	3,027	
8. Illness/Accident Insurance	<ul style="list-style-type: none"> Canberra Cabs calculate on 75% of owner-driver gross income of \$62,880 pa, but this over-states the loss if owner-driver unable to drive. based on net income being 50% of gross income, appropriate amount could be half this. But allowing for fixed costs, take 75% of CC figure. 	2,028	-	