Taxi Fare Methodology Inquiry

Final Report

May 2013

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EXECUTIVE SUMMARY

The Regulator was requested by the Minister of Finance and the Transport Commission to consider the method for setting fares, the indexation of fares and the relative weighting of fare related components. The full terms of reference can be found at Attachment A.

To assist in the inquiry, the Regulator engaged the services of the consultancy firm the Centre for International Economics (CIE). The CIE has prepared a final report which accompanies this Final Report.

In preparing the Final Report, the Regulator took into consideration the CIE's final report, input from stakeholders through consultation and OTTER staff research. The release of this Final Report and the CIE's final report signifies the completion of this inquiry.

The Regulator has made a number of recommendations aimed at improving the taxi fare setting process which at present the Regulator considers is characterised by inconsistencies in its application and based on incomplete information.[1] The Regulator notes that there appear to have been multiple reviews undertaken into the taxi industry over the past decade but with respect to fare setting limited improvements appear to have been made.

In this light, the Regulator is recommending a staged approach to implementing its recommendations to assist in facilitating meaningful progress for the benefit of passengers and the industry.

Stage 1: Adoption of new taxi cost indices and a consistent transparent process

Stage 1 involves moving to a new model for fare setting and adopting a regular and transparent process for fare reviews and adjustments.

In terms of the model to be adopted, the Regulator recommends:

- new taxi cost indices be adopted as outlined in Table 1 separately for Hobart, Launceston and other areas of Tasmania;
- that the cost weights in the models be inflated each year by independent publicly available estimates for inflators as outlined in Table 1; and
- that the final output from the cost model be adjusted for productivity based on a gross output measure of multi-factor productivity using a 10 year average.

[1] See the CIE (2013) "Setting taxi fares in Tasmania" Final Report, p.25.

In terms of the process for undertaking fare reviews, the Regulator recommends:

- consistent periodic reviews of fares be undertaken (as opposed to the current ad hoc approach);
- fares should be adjusted annually in line with movements in the taxi cost indices and productivity adjustments;
- major reviews should occur every four years that re-examine the cost weights in the model;
- taxation and regulatory changes outside of the model should be passed through fares to the taxi industry;
- fuel prices should be monitored six-monthly with fares adjusted should fuel price movements lead to an overall cost change of more than three per cent between annual reviews;
- up to two rounds of consultation be undertaken during major reviews with no consultation undertaken during annual reviews when the mechanical cost indices are updated;
- an independent body should undertake all future taxi fare reviews including major four-yearly reviews, annual indexation adjustments and six-monthly fuel monitoring; and
- licence fees should be adjusted as necessary to fund this new fare setting process.

The Regulator considers that these recommendations can be readily implemented by the Government and considers it prudent to expedite the implementation of these recommendations.

Table 1: Recommended cost weights and indexation factors

Cost	Cost Shares			Indexation factor
	Hobart	Launceston	Other	All
	Per cent	Per cent	Per cent	
Radio room costs	6.0	6.9	15.6	ABS CPI, Communications for Hobart
Vehicle costs (including fit out)	4.0	4.5	5.7	ABS CPI Motor Vehicles Hobart and RBA small business indicator rate for variable loans
Servicing, maintenance and repairs	6.3	6.7	6.8	ABS Consumer Price Index for maintenance and repair, Hobart
Insurance	4.0	4.2	4.3	ABS CPI, Insurance for Hobart
Registration	1.1	1.2	1.7	Government regulated fees[2]
Operator labour	4.1	4.3	4.4	ABS Wage Price Index for Tasmania (Public and Private)
Plate leases	11.0	8.1	4.5	0 per cent
Driver labour	50.0	50.0	42.5	ABS Wage Price Index for Tasmania (Public and Private)
Fuel	13.5	14.1	14.5	Average annual percentage change in fuel costs for Hobart from Fueltrac
Total	100.0	100.0	100.0	

Source: The CIE.

Stage 2: Adjustments to fare structure and de-regulation

The Regulator considered the adequacy of the current fare structure and proposals for fare structure changes made by the industry. These considerations primarily surrounded:

- whether the flagfall should be raised and the distance rate lowered to incentivise more drivers to undertake shorter trips;
- whether a tariff three should be implemented for late nights shifts between 11 pm and 6 am;
- whether a separate surcharge should be applied on special event days outside of Hobart and Launceston; and
- whether the fare setting process should be partially de-regulated using a weighted average price cap.

[2] The change in cost for this item will be observed based on the regulated fees set by DIER and the MAIB. See http://www.transport.tas.gov.au/fees/calculation_of_fees_-_class_a_vehicles and http://www.maib.com.au/premiums.

The Regulator considers that there is merit in applying a surcharge on special events days, consistent with the late night surcharge in the *Taxi Industry Regulations 2008*. This would assist taxi operators with the higher cost per trip associated with special event days that may prevent operators sharing more fare revenue on these days to attract drivers.

However, with respect to other fare structure changes, the Regulator considers that it has insufficient information at present to assess and make changes to the current fare structure. The Regulator considers that de-regulation via the use of a weighted average price cap may be an appropriate consideration in the future because the taxi industry understands its industry conditions and client base best and may be in a better position to adjust fares to its benefit, subject to constraints placed on it by the Regulator to protect consumers and promote efficient outcomes. However, at present the taxi industry would prefer that fares remain fully regulated. Furthermore, the Regulator does not consider it has sufficient information on the length of the average taxi journey during different times of the day to adopt this approach at this stage.

One difficulty with receiving data is that the Tasmanian taxi industry currently is not represented by an industry body. Given this, the Regulator has received some limited information from a few operators but does not consider it has an accurate enough picture of the overall industry to make such fare structure changes.

In order to consider a fare structure change in the future, the Regulator considers that more detailed data would be required from a broader array of stakeholders across the industry. This data may include the number of trips, average distance travelled and revenue earned by time of day, day of the week and by taxi area, waiting times and missed trips.

The Regulator considers that if this were to occur, it would be in a much better position at the next taxi fare review to consider what adjustments to the fare structure should occur to the benefit of passengers and the industry.

Stage 3: Treatment of plate lease costs

The Regulator has outlined in this Final Report its concerns about how plate lease costs are currently treated and how the Regulator considers they should be treated in the models.

The Regulator considers that when regulating prices for any industry these prices should be based on the efficient economic cost of providing a good or service. This usually involves setting prices that allows a regulated entity to earn a reasonable rate of return and be financially viable.

The difficulty with the taxi industry is that fares currently recover efficient economic costs plus a financial cost in terms of rental payment to plate lease owners. Lease costs are not an efficient economic cost rather the lease cost represents the financial value of plate leases that arises due to restrictions on the supply of lease plates, known as an “economic rent”. In other regulated industries, regulators keep a check on potential economic rents by only allowing for efficient economic costs to be included when determining prices.

The further difficulty in the taxi industry is that this economic rent has largely been created by successive governments restricting the supply of licences. This has created a market for individuals to purchase and own lease plates as an investment but not operate taxis themselves. As with any investment, investors expect a rate of return on that investment (and funds to assist in paying off loans that may have funded that investment), which is provided through the lease payments paid by operators. This cost though is funded by consumers through higher fares.

If the Regulator were to adopt a normal economic and regulatory approach, it would lead to a deflation in the value of plate leases and may place some plate lease owners under financial duress. The Regulator notes that this particular issue has received considerable attention in recent years following taxi reviews in both NSW and Victoria.

Balancing these concerns, the Regulator recommends that the inflationary factor applied to plate lease costs in the taxi cost indices should be set at zero per cent for the next four years until the next major review. Adopting this method would ensure that any increase in the value of licences would not be passed through fares to consumers. Furthermore, fare regulation would not directly impact the nominal value of licences (in real terms this approach will lead to a decline in real value because additional revenue is not provided to allow for an increase in the nominal value of licences).

However, in the longer-term the Regulator considers that the Government needs to give strong consideration to its position on this issue and provide direction for both fare regulation and licence releases for the next major fare review. DIER has indicated that its policy position is to take into account the interests of consumers on this issue and that lease costs should be deflated in the taxi cost index over time. However, as outlined in this report, the Regulator considers that, to date, there does not seem to have been any apparent correlation between the policies relating to fare regulation and licence releases and DIER's position with respect to consumers. Given this, and without knowing what the Government's policy will be following the completion of DIER's current licence release review, the Regulator considers it prudent to apply a zero per cent inflator until further direction is provided by government.

1 INTRODUCTION

1.1 Inquiry process

The Regulator received an official request from the Minister for Finance on 31 August 2012 to undertake a taxi fare methodology inquiry. The inquiry has been requested by the Transport Commission and has been endorsed by the Minister for Sustainable Transport. The Regulator was requested to consider the method for setting fares, the indexation of fares and the relative weighting of fare related components. The full terms of reference can be found at Attachment A.

To assist in the inquiry, the Regulator engaged the services of the consultancy firm the Centre for International Economics (CIE). The CIE has prepared a final report which accompanies this Final Report.

In preparing the Final Report, the Regulator took into consideration the CIE's final report, input from stakeholders through consultation and OTTER staff research. The release of this Final Report and the CIE's final report signifies the completion of this inquiry, as highlighted in the table below.

Milestone	Date
Release of Terms of Reference	31 August 2012
Engage the CIE	1 October 2012
Initial consultation	November 2012
Receipt of the CIE's draft report	December 2012
Release of the Regulator's Consultation Paper and the CIE's draft report	15 February 2013
Submissions due	3 April 2013
The Regulator's report submitted to the Transport Commission, Minister for Finance and Minister for Sustainable Transport	31 May 2013

1.2 Final Report Recommendations

The Final Report makes a number of recommendations aimed at improving the process for taxi fare regulation. This includes a number of recommendations that the Regulator considers should be implemented immediately followed by a number of other recommendations that require government policy input and future data and input from the taxi industry. The Regulator suggests these other recommendations should be further investigated at the time of the next major review, notionally suggested to be in four years time.

1.3 Structure of the Final Report

This Final Report has been prepared to assist the government in considering an improved process for regulating taxi fares. The paper is structured as follows:

- Chapter 2 provides an overview of the taxi industry and the current fare setting arrangements;
- Chapter 3 discusses the objectives of setting taxi fares in Tasmania;
- Chapter 4 discusses the current fare structure and options for possible improvement;
- Chapter 5 discusses what should be included in a model for fare setting and presents proposed weights for cost indices for a representative taxi for specific areas in Tasmania;
- Chapter 6 discusses possible methods for indexing cost items in the cost indices, including the specific items of plate leases, driver labour costs and a productivity adjustment; and
- Chapter 7 discusses possible future arrangements for setting fares.

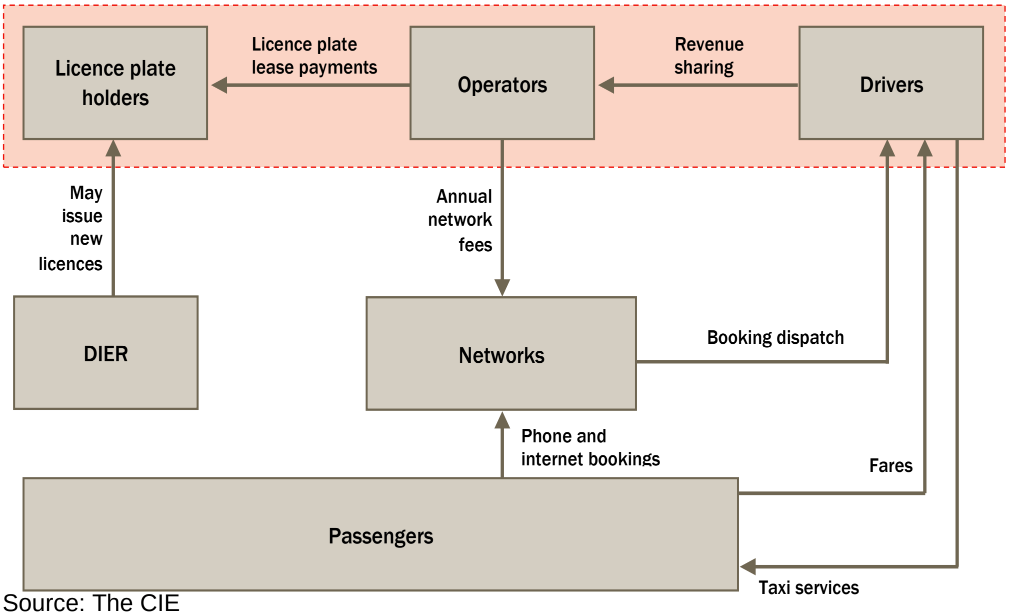
2 TAXI INDUSTRY OVERVIEW[3]

This section provides a brief overview of the taxi industry in Tasmania including the structure of current fares.

2.1 The taxi industry in Tasmania

The Tasmanian taxi industry involves many players and the relationships between these players can be complex. In some cases a single organisation (or individual) can be involved in multiple parts of the supply chain, whilst in others it is separated out into distinct components. The relationship between taxi industry players is summarised in Figure 2.1.

Figure 2.1: Relationship between taxi industry players



Source: The CIE

Taxi operators are required to hold a licence plate issued by the Department of Infrastructure Energy and Resources (DIER). There are four different types of licences:

- a perpetual taxi licence, which as the name suggests, continues indefinitely;
- an owner-operator taxi licence that must be operated by the person owning the licence and hence the owner must be an accredited operator;
- a wheelchair accessible taxi (WAT) licence; and

[3] This chapter has been recreated from the CIE's final report.

- a temporary taxi licence, which expires after a period of time, cannot be traded and can only be issued to an accredited operator.

Taxi licences also apply to specific taxi areas, of which there are 24 in Tasmania.

Perpetual licence plate holders can either operate a taxi themselves or earn a rate of return on their asset by leasing the licence plate (known as a plate lease) to a separate operator, depending on the type of licence. Operators are responsible for various costs associated with operating a taxi, including purchasing or leasing the vehicle, vehicle maintenance, insurance and network fees. Operators can drive the taxi themselves or hire a driver (or both).

The Regulator understands that there are currently 567 licences in Tasmania comprising:

- 448 perpetual licences;
- 56 owner operator licences; and
- 63 WAT licences.

Furthermore, there are four networks in Hobart and one in Launceston whilst co-op arrangements exist in other areas of Tasmania.

In Tasmania, fare revenue is generally split between the operator and the driver based on an agreed percentage (normally on a 50:50 basis). The Regulator understands that these arrangements are not regulated. Consultation suggests that the share of revenue returned to taxi drivers can be as low as 40 per cent.

The arrangements for supplying taxi services can vary considerably. In some cases, the licence plate holder, the operator and the driver may be the same person. In other cases they may be completely separate.

Passengers can obtain a cab from either:

- a taxi rank;
- by hailing one down on the street; or
- by booking over the telephone, via the internet with an authorised taxi network or through smart phone applications.

In Tasmania, based on information provided during the initial consultation phase, the Regulator understands that as much as 80 per cent of taxi services are provided through bookings.

2.2 Taxi fares in Tasmania

The 24 licence areas fit into three different fares bands:

(a) Hobart, Launceston, Devonport, Burnie, West Tamar, Ulverstone and Perth;

(b) King Island and Flinders Island; and

(c) other areas not listed in (a) and (b).

WATs can also charge different fares for passengers that require wheelchair accessibility, although this is currently being reviewed, separately by DIER.

Current taxi fares are set out in Table 2.1.

Table 2.1: Current taxi fares

Fare component	Major areas[a] $	Other $	King/Flinders Island $
Flagfall	3.40	3.40	4.90
Tariff 1 (per km)	1.84	1.81	2.05
Tariff 2 (per km)	2.20	2.17	2.46
Waiting time (per hour)	36.26	35.31	41.49

[a] Hobart, Launceston, Devonport, Burnie, West Tamar, Ulverstone and Perth

Source: DIER

The process for setting taxi fares currently takes the existing level and structure of fares and focuses on the change that should be applied to this. The change in fares has been made using either the CPI or a cost index since 2003. More details about the current arrangements are outlined in Chapter 3 of the CIE's final report.

3 OBJECTIVES OF TAXI FARE REGULATION

This section discusses the objectives of taxi fare regulation which is an important preliminary step in determining a methodology for setting fares. Without clear objectives, there is a greater risk of incurring unintended outcomes not desired by policy makers and stakeholders. Thus clear objectives are required to ensured a methodology is developed with the aim of achieving those objectives.

The CIE in their final report considered the objectives of taxi fare setting regulation in general and specifically in the Tasmanian context. In reviewing these objectives, the CIE concluded that in Tasmania:

> "There is a lack of clear objectives and process in the fare setting process".

In considering possible objectives for the Tasmanian taxi industry, the CIE reviewed:

- international and Australian best practice guidelines for regulation including from the OECD, COAG, the ACCC and the UK Department for Business Innovation and Skills;
- pricing principles specific to the taxi industry with reference to NSW;
- the intent of the *Taxi and Luxury Hire Car Industries Act 2008*[4]*;* and
- undertook initial consultation with government stakeholders and industry in Tasmania.

Based on this review the CIE suggested that the objectives of taxi fare regulation in Tasmania should be as follows:

> "The objectives of taxi fare regulation should reflect the interests of consumers. This is consistent with the principles of economic regulation more generally and with the intent of the *Taxi and Luxury Hire Car Industries Act 2008*. Fare regulation should:
>
> - aim to set fares that are economically efficient, both in terms of level and structure. Specifically, the regulated fares should seek to:
>   - reflect the efficient cost of providing the service;
>   - protect consumers from the abuse of market power;
>   - ensure that there are no cross-subsidies between groups of customers;

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[4] The intent of this Act is, in respect of taxi services, to ensure the provision of a safe, demand responsive, taxi transport system in Tasmania that adequately meets the needs of consumers.

- allow a standard of service, including availability and safety, that consumers are willing to pay for; and
- provide incentives for the industry to improve efficiency."

The above objectives focus on the consumer of taxi services.

Another common objective in economic regulation is the viability of the industry that is being regulated. In this light, Section 31 of the *Economic Regulator Act 2009* outlines matters to be considered by the Regulator when undertaking investigations of monopoly providers. Section 31 of the Economic Regulator Act notes that in a monopoly provider investigation, the Regulator is to consider the following matters:

- if appropriate, the need for a reasonable return (including the payment of dividends) on the assets of a monopoly provider (Section 31 (d)); and
- the need for the monopoly provider to be financially viable (Section 31 (g)).

These matters are to be considered in conjunction with other matters related to protecting consumers from the adverse effects of the exercise of monopoly power. The intention of the above clauses is generally to ensure prices are not set so low that they may compromise the ability of the industry to continue to provide reasonable services.

Through the initial consultation with stakeholders, industry viability was a matter raised by stakeholders.

The CIE considered that industry viability was important "only insofar as it ensures that customers receive a service that meets their needs". [5]

This view is generally consistent with broader regulatory precedent (and the matters noted above in the Economic Regulator Act). This is because if prices are regulated to recover efficient costs then:

- industry will cover all of its costs;
- industry will obtain a return commensurate with a competitive market outcome; and
- industry will be financially viable.

The difficulty with the taxi industry is that by setting a price that recovers the efficient cost of providing services this may put at risk the financial viability of some players in the industry.

This is because taxi fare revenue is currently used to recover more than the efficient cost of operating a taxi. Taxi fare revenue currently is used to pay rental payments to lease plate owners. However this plate lease cost is not an efficient economic cost. Rather, the plate lease cost represents the financial value of plate leases that

[5] See The CIE (2012) "Setting taxi fares in Tasmania" final Report, p.19.

arises due to restrictions on the supply of lease plates, known as an “economic rent”. If the market for lease plates was competitive and there were no restrictions on supply, new entrants would enter the market thereby reducing the value of lease plates, lease costs to operators and ultimately fares. In other industries, regulators keep a check on potential economic rents by only allowing for efficient economic costs to be included when determining prices.

The difficulty in the taxi industry is that this economic rent has largely been created by governments by restricting the supply of licences. This has created a market for individuals to purchase and own lease plates as an investment but not operate taxis themselves. As with any investment, investors expect a rate of return on that investment (and funds to assist in paying off loans that may have funded that investment), which is provided through the lease payments paid by operators. This cost though is funded by consumers through higher fares.

The Regulator recognises that this is a difficult issue and one which has received considerable attention in NSW and Victoria over the past year.[6] Possible ways of addressing this issue are discussed in Section 6.2 but a decision on how to address it will be impacted by the objective taken with respect to plate lease.

Consultation

The Regulator invited submissions on the following matters with respect to the objectives of taxi fare regulation:

- stakeholder comments on the CIEs suggested objectives of taxi fare regulation in Tasmania; and
- should maintaining the value of taxi plates, and in turn the value of lease payments in relation to those plates, be included as an objective in setting taxi fares?

Submissions

All submissions endorsed the CIE’s recommended objectives, however there were mixed views concerning the treatment of lease payments and taxi plate values.

The Department Infrastructure, Energy and Resources (DIER) considered that it is not appropriate for a regulator to have a role in underpinning the value of taxi licences. DIER stated that under current legislation the Transport Commission is obliged to offer additional licences for sale each year. As such, the long term maintenance of the scarcity value of taxi licences is not an objective of the licensing regime. Thus in DIER’s view the introduction of plate value maintenance as part of the fare setting process would be directly contradictory to the objectives of the broader licensing scheme. DIER considered that only an appropriate return to an

[6] See IPART (2012) “Review of Taxi Fares in NSW, Maximum Fares from July 2012 Final Report”, IPART (2012) “Annual Taxi Licence Release for Sydney 2013/14 Draft Report” and Taxi Service Commission (Victoria) (2012) “Customer First: Safety, Service, Choice – Taxi Industry Inquiry Final Report”, December 2012.

efficient operator should be allowed. Whilst DIER do not define what an appropriate return is, it indicated that it is not one that includes rents based on scarcity value.

Yellow Cabs in Hobart and Taxis Combined in Launceston both consider that the direct costs associated with plate leases (weekly rental arrangement) should be taken into account when setting fares. They consider that the market should be allowed to dictate the value of a Perpetual Licence and in turn the weekly rental payment.

This view is supported by a stakeholder in the Burnie/Wynyard taxi area who considers that the investor takes a risk when investing and the value of the asset should be determined solely by market forces. This stakeholder does not consider maintaining the value of taxi plates or lease payments should be an objective in setting taxi fares, however maintaining a viable taxi industry should be an objective.

Finally, Yellow Cabs in Hobart and Taxis Combined in Launceston both consider that if a change was made that impacted directly on the owner of a Perpetual Taxi Licence owner and the plate lease cost the Government should provide compensation accordingly. They point to the experience in the Northern Territory where plates were bought back by the government and leased back to the industry for a small fee.

Regulator’s conclusion

The Regulator considers that this is a material issue that requires policy direction from government.

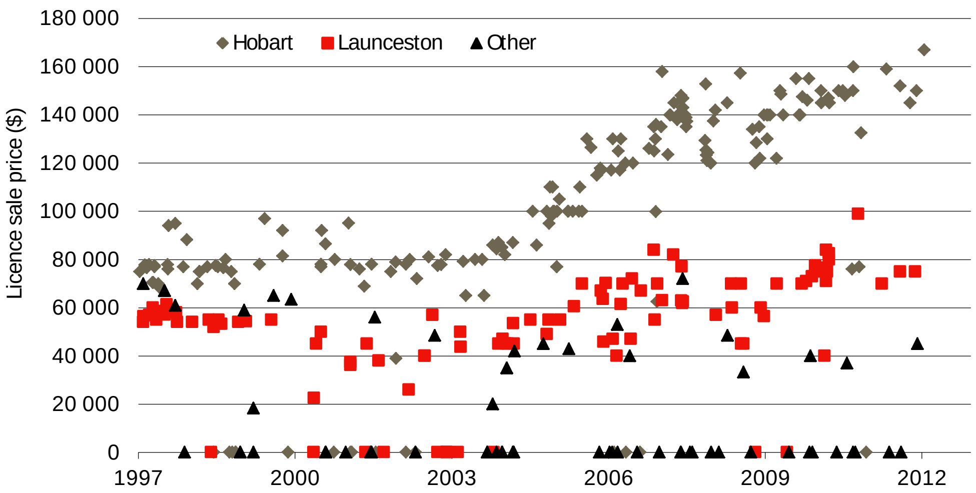
If the Regulator was asked to undertake taxi fare regulation, it would be guided by the rules put in place by government to guide any review. These rules would normally be outlined in the relevant Act and/or terms of reference provided by the government. In the absence of such instruction, it would be left to the Regulator to consider the appropriate objectives and balance the views of competing stakeholders. If the Regulator were to follow a similar approach as adopted with the other industries it regulates, this may mean reducing the impact of weekly lease payments on fares over time.

The Regulator considers that, to date, there does not seem to have been any apparent correlation between the policies relating to fare regulation and licence releases and DIER’s position with respect to consumers.

The Regulator considers that the current method of taxi fare regulation, which excludes plate leases from the model, inadvertently contributes to the increase in the value of licences. This is discussed in more detail in Section 5.1.

Furthermore, the Regulator does not agree that the on-going annual release of licences is necessarily inconsistent with the long term maintenance of the scarcity value of taxi licences. Whilst the Regulator agrees that maintaining the value of licences has not necessarily been the goal of the Transport Commission, perpetual licences have increased in value as outlined in Figure 9.4 in the CIE’s final report and reproduced below. The Regulator understands that a larger number of licences were released between 2007 and the present which has stemmed the increase in licence values, but licence values have not fallen. Recent licence releases may therefore be considered maintenance releases that keep up with on-going demand without addressing the issue of scarcity value.

Figure 3.1: Licence sale prices by jurisdiction



Source: Tasmanian Department of Infrastructure, Energy and Resources.

This issue is difficult to resolve without a policy setting in place by government on the value of licences. It is acknowledged that DIER is currently undertaking a review of licence releases and that the outcomes of the review may provide clarity on the policy objectives in relation to lease plate value.

4 FARE STRUCTURE

This section discusses options for structuring taxi fares including how cost increases may be applied to the components of fare increases.

The current fare structure splits charges between the following items:

- Flagfall – which is the amount on the meter when the taxi is hired;
- Distance rate – a kilometre based charge for the distance travelled in a taxi. There are two kilometre based charges for different times of the day (one between 6am and 8pm and, a second higher charge, between 8pm and 6am); and
- Waiting time - which is added to the fare instead of the distance rate when the taxi is stopped, or travelling at less than a particular speed.

While there are slightly higher charges between the different taxi zones of Tasmania and for WATs, the charging structure remains the same.

Initial consultation with the taxi industry suggested that the majority of the industry may be satisfied with the existing structure of fares.

However, the CIE noted some alternative options to consider in structuring fares. These are discussed in more detail below.

4.1 Higher flagfall

From the initial consultation with industry the Regulator understands that it may be difficult to access a taxi in certain suburban areas. Drivers may be discouraged from pick-ups in suburban areas for a number of reasons including that the value of fares in such areas is too low. This is because many passengers may only want a short trip within a suburban area which would attract a low distance based charged. As such, drivers received a small return for their work within suburban areas and may wish to remain in busy city areas or at the airport where than can attract a higher fare.

A possible solution to this problem is to increase the flagfall relative to the distance based charge to provide for a greater return on short trips. In theory this may provide for greater access of taxis in suburban areas that attract smaller trips.

However, the Regulator also understands that many taxi users in suburban areas are pensioners and low income earners. Given this, many of these users may not be able to afford the higher fares that would result from this fare structure. Furthermore, the Regulator appreciates that some low income customers such as pensioners may prefer the certainty of lower fixed fees. Thus whilst a higher flagfall may provide for greater supply of taxis in suburban areas, demand for taxis may fall.

Setting the appropriate flagfall level would therefore appear to be about balancing accessibility of taxis with affordability for lower income earners.

Consultation

With respect to the flagfall, the Regulator asked stakeholders:

- is access to taxis within suburban areas an issue; and
- should the flagfall charge be raised (and the distance based charge reduced in proportion) to encourage more drivers to operate within suburban areas?

Submission

Stakeholders had mixed views on this issue.

Yellow Cabs and Taxis Combined Launceston considered that the flagfall should be raised to attract drivers to undertake shorter trips. Yellow Cabs and Taxis Combined noted that both the relatively low revenue received from short suburban trips and the less chance of receiving a return trip both act as a disincentive for drivers. These entities consider that the flagfall should be raised to $4 to compensate for this. Furthermore, they consider it should be raised by any extra two dollars for late night shifts to compensate for working during less desirable and more dangerous periods (see Section 4.4 for further discussion).

However, another stakeholder in the Burnie/Wynyard area considered that attracting drivers to shorter trips was not an issue in their licence area. This stakeholder considered that the current level for the flagfall was reasonable.

Regulator's conclusion

The Regulator considers that there is insufficient evidence and support from the industry to increase the flagfall at this stage. This is because:

- direct support for increasing the flagfall was only expressed by one network in Hobart and one in Launceston;
- data is limited on what any increase in flagfall should be and simultaneous decrease in the distance charge to maintain the current revenue level based on current demand;
- it is unclear whether increasing the flagfall would lead to a more economically efficient; and
- through initial consultation concerns were expressed to the Regulator by TasCOSS (who represent low/fixed income groups) about undertaking such an approach.

That said, the Regulator encourages the taxi industry to collate and provide more detailed information for consideration at the next major review. This is discussed in more detail in Section 4.8.

4.2 Booking fee

In many other jurisdictions customers who pre-book a taxi are charged a booking fee. The rationale for the booking fee is to compensate the driver for the costs involved in getting to the passenger. A booking fee may also assist some customers that may find it difficult to obtain a taxi perhaps due to their location or those customers seeking a short trip only.

However, there are complications in setting the booking fee because the costs involved in travelling to pick up passengers will vary depending on their location. Furthermore, the Regulator understands that up to 80 per cent of fares are currently booked in Tasmania. The CIE notes that since most passenger trips are booked through the network, the distinction between implementing a booking fee and raising the flagfall is diminished.[7] Indeed, if a booking fee was introduced, it would need to be off-set by reductions in other fare components such that it did not increase the overall fare level.

Consultation

The Regulator asked stakeholders if they saw the need for a booking fee.

Submission

Stakeholders again had mixed views on this issue. Yellow cabs and Taxis combined Launceston considered that there may be merit in introducing a booking fee to attract drivers to suburban trips. However, another stakeholder in the Burnie/Wynyard area considered the cost of administering a booking fee does not warrant its introduction and with about 80 per cent of jobs coming through the taxi base a more efficient response would be to incorporate any cost into the flagfall.

Regulator's conclusion

The Regulator considers that a booking fee is unnecessary due to:

- the link between the booking fee and the flagfall in markets with a relatively large amount of bookings;
- limited support at present from the industry; and
- the introduction of a booking fee would increase the complexity of the fare structure and consideration would need to be given on how best to reduce the other fare components to ensure that the taxi industry receives the same amount of revenue on average. The Regulator does not consider that it has sufficiently robust information to undertake this analysis at this time.

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[7] See The CIE (2012) "Setting taxi fares in Tasmania" Final Report, p.45.

4.3 Tariff 2

In Tasmania a higher distance based charge (Tariff 2) is charged between 8pm and 6am on weekdays and all day on weekends and public holidays. This charge is approximately 20 per cent higher than Tariff 1. DIER notes that "This increase in fares leads to a corresponding increase in driver revenue, which may serve to offset the negative aspects of working at less attractive times".[8]

In NSW, a night time surcharge is charged rather than a broader Tariff 2 as applies in Tasmania. The Independent Pricing and Regulator Tribunal (IPART – the body responsible for regulating taxi fares in NSW) noted that that rationale for the night time surcharge is:

- to compensate drivers for periods of lower demand;
- to raise taxi earnings in night periods to compensate drivers for unsocial hours; and
- to help ensure a reasonable level of taxi supply in night periods.[9]

However, this surcharge has been restricted to the night time. This is because in NSW IPART considers that there is no evidence of a shortage of supply of taxis during the day on weekends in urban areas. IPART also considers that there is also insufficient evidence to suggest that a fare premium is required to compensate drivers for additional safety risks involved in working during the day on weekends and public holidays as is the case with late night driving.[10]

The CIE, in its final report, indicates that evidence from other States suggests that the relationship between the level of fares and drivers compensation is weak.[11] The CIE notes that the impact of higher fares on driver earnings could potentially be eroded by a range of factors including:

- less demand due to the higher fares;
- more taxis on the road competing to receive the higher fares; and
- higher payments to operators, with some drivers willing to receive less than the current 50 per cent share of fare revenue.

The CIE notes that raising Tariff 2 may not actually increase driver earnings to any significant extent, raising the question of whether it is actually needed, particularly during the non-peak times when Tariff 2 is active. The CIE also notes that the period during which higher tariffs apply is somewhat arbitrary and appears to vary

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8 DIER (2005) "Review of the Taxi and Luxury Hire Car Industries Act 1995, *Paper 2 – Taxi Fare Setting and Driver Pay and Conditions*" December, p.41.

9 IPART (2012) "Issues Paper: Review of Taxi Fares in NSW, Maximum Fares from July 2012", p.32.

10 IPART (2012) "Review of Taxi Fares in NSW, Maximum Fares from July 2012 Final Report", p.53.

11 See The CIE (2012) "Setting taxi fares in Tasmania" Final Report, p.46.

significantly across States. There may be a case for higher tariffs in peak periods, such as Friday and Saturday nights.[12]

Consultation

With respect to Tariff 2 stakeholders were asked:

- if they believe a Tariff 2 is required in Tasmania; and
- if so, is the current timeframe appropriate and/or should it be shortened or lengthened?

Submissions

Stakeholders considered that a Tariff 2 is required for Tasmania for the following reasons:

- due to the danger faced by drivers during night time shifts;
- to cover additional expenses at night time including replacing windows, repairing damaged body work, stolen property inside taxis and to compensate for fare evasion;
- for penalty rates for drivers working night times, weekends and public holidays similar to other industries; and
- to provide a financial incentive for operators and drivers to work on high cost days.

Stakeholders also considered that shortening the period over which Tariff 2 operates, and a commensurate increase in the period for Tariff 1, was in appropriate given their concerns outlined above. Rather one stakeholder indicated that Tariff 2 should be extended to start at 7pm rather than 8pm to be consistent with penalty rates with the rest of the economy.

Yellow Cabs and Taxis Combined Launceston considered that Tariff 2 should apply from 6pm to 11pm Monday to Friday and during the day on weekends, public holidays and bank holidays. In addition, these entities considered a new Tariff 3 should be implemented between 11pm and 6am every day (see Section 4.4).

Regulator's conclusion

The Regulator considers that the inclusion of Tariff 2 in the fare structure is sensible to cover the additional costs during night time shifts and to provide compensation to the industry for operating outside of normal business hours.

However, similar to the reasons outlined with respect to increasing the flagfall, the Regulator considers that there is insufficient information i.e. from a broader representative group of stakeholders to warrant a change from the existing Tariff 2

[12] Ibid pp.47.

arrangement. Section 4.8 provides more detail on what the data requirements may be in the future.

4.4 Tariff 3

During the initial consultation, stakeholders suggested a new Tariff 3 should be considered for particular times when it is difficult to source drivers. This Tariff 3 could apply broadly to late night weekend shifts and public holidays or for specific times of the year when there is sufficient evidence that attracting drivers is difficult.

If Tariff 3 is applied broadly it may have the same impact on driver income as discussed above in section 4.3. This may suggest that the objectives of introducing a broad based Tariff 3 would be better addressed through adjustments to Tariff 2 perhaps by shortening the length of time Tariff 2 applies for and possibly increasing its level. In this manner, drivers would be compensated for shifts that may involve unsociable hours or be more likely to attract unsavoury or violent passengers.

A specific Tariff 3 may have the advantage of specifically targeting those particular days of the year in which driver supply is particularly weak. From the initial consultation the Regulator understands that these days include Christmas Eve, New Years Eve and AFL grand final day. The Regulator understands that in Western Australia a surcharge is applied between 12am and midnight on Christmas Day and between 6pm and 6am New Years Eve/Day.[13]

Alternatively, given that there may be only few instances of this, the Regulator considers that perhaps it should be left to industry to determine how best to serve consumers on these days. This may mean if operators would like to attract more drivers then they may need to provide a greater share of fare revenue during these particular shifts.

Consultation

With respect to Tariff 3 the Regulator asked stakeholders:

- when it should apply;
- what days of the year it should be applied to; and
- what should the value of Tariff 3 be?

Submissions

Similar to Tariff 2, stakeholders considered that there is merit in introduction a Tariff 3 to compensate drivers and operators working unsociable hours. However, stakeholders provided different proposals on the application of a Tariff 3.

One stakeholder considered that it should be used for special event days, specifically Christmas Eve, Christmas Day, New Years Eve and AFL grand final day.

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[13] See http://www.transport.wa.gov.au/taxis/15154.asp

These times tend to be the most difficult to attract drivers and cost the most in terms of damage to taxis. This stakeholder considers that these additional costs make it difficult to afford to provide additional fare revenue to drivers on these shifts. This stakeholder proposes an additional surcharge of two to three dollars per trip on these occasions, noting that many of the patronage have spent discretionary income on entertainment and alcohol and thus can afford it.

Alternatively Yellow Cabs and Taxis Combined Launceston consider that a broader Tariff 3 should apply all year round from 11pm to 6am each day. Similar to above, these entities consider an additional premium on the flagfall should be added.

Regulator's conclusion

Similar to the Tariff 2 and flagfall discussion, the Regulator considers that at present there is insufficient information to warrant changing the current fare structure to include a new broad based Tariff 3 as proposed by Yellow Cabs and Taxis Combined Launceston. Section 4.8 provides more detail on what the data requirements may be in the future.

The Regulator considers that there is merit in applying a specific premium to tariffs on special events. Section 6(1) of Schedule 3 of the *Taxi Industry Regulations 2008* allow taxi operators to charge customers a surcharge of $2.60 per trip between the hours of 12:30am and 5am. The Regulator considers that this should be amended, or a sub-clause included, allowing operators to charge customers this surcharge on Christmas Eve, Christmas Day, New Years Eve and AFL grand final day.

4.5 De-regulation of fare components

In their final report, the CIE raised an option of setting the maximum fare for an average trip and allowing industry to determine their own fare structure. Under this approach the regulator could determine the maximum amount of revenue that could be earned from an 'average trip'. Following this, each network owner/operator would submit to the Regulator their proposed fare structure that would recover the same revenue on this average trip. This would involve a decision, at minimum, on the relative size of the flagfall and the distance based charge.

For example, the CIE noted that the current average fare may be $19.33 based on an average trip specified as eight kilometres with two minutes of waiting time. If average costs rose by three per cent, this would increase to $19.90. In a de-regulated fare structure environment, network operators would be able to set their flagfall anywhere between $0 and $19.90 and their corresponding distance charge anywhere between $2.50 per kilometre and $0 so long as the value of the average trip was still $19.90. Using these extremes, a one kilometre fare could range between $2.50 and $19.90 and a 25 kilometre trip could range from $19.90 to $62.20 depending on the fare structure chosen by the network operator. The CIE in its final report acknowledge that "while large fare differentials would be possible in a de-regulated environment, it is also unlikely. It is more likely that all networks would choose a fare structure somewhere between these extremes".[14]

The logic behind this approach is that operators are closer to the industry and thus may be better placed to determine the optimal fare structure. The CIE notes that this is conceptually similar to the weighted average price cap approach that has been widely applied to regulator decisions in other industries.[15] A weighted average price cap form of regulation is noted as being welfare improving for consumers and producers in a natural monopoly setting and the Australian Energy Regulator adopts this approach for monopoly electricity distribution companies. The Australian Energy Regulator notes that the weighted average price approach provides the highest incentive for efficient prices of the alternative forms of regulation that it has considered.[16] This would suggest that perhaps a weighted average price cap may be appropriate for some monopoly providers of taxi services in Tasmania.

However, in NSW, IPART determines a weighted average price cap for its regulation of electricity retailers which is not in a natural monopoly setting. Each year regulated electricity retailers submit a tariff structure that matches this weighted average price cap based on their expectation of the numbers of customers served and the volume of demand. Furthermore, each year IPART allows for a weighted average price increase and regulated retailers are free to adjust their regulated tariffs as long as the new weighted average price cap is met. This can potentially lead to large fluctuations in individual tariffs. However, IPART note that they believe there is sufficient competition in the metro NSW market to ensure these fluctuations are minimal and subject to competitive pressures.[17] Indeed this process appears to have been effective since it was introduced in 2007.

Based on this logic, this would suggest that a de-regulated fare structure may be suitable for consideration in Hobart where there are four network operators currently. Consumers would have the ability to decide to book a taxi with a different operator if they did not like the fare structure on offer from a particular operator. Hence this competitive pressure would ensure that all network operators set what they perceive to be an optimal fare structure to compete with each other for the available demand.

However, as discussed above, the theory of weighted average price cap regulation has focused primarily within the natural monopoly setting. The CIE note that in a competitive taxi industry there may be complex interactions between pricing policies chosen by different networks that may influence the effectiveness of a weighted average price cap. For example, if some taxis were able to effectively target

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[14] The CIE (2012) "Setting taxi fares in Tasmania" Final Report, p.86.

[15] Ibid p.43.

[16] See Australian Energy Regulator (2012) "Matters relevant to the framework and approach, ACT and NSW DNSPs 2014-19: control mechanisms for standard control electricity distribution services in NSW and the ACT" April, p.9.

[17] See IPART (2012) "Review of regulated retail prices and charges for electricity 2013 to 2016 – Issues Paper". pp.36-37

particular segments of the market (e.g. longer trips) and set their fares accordingly, they may be able to benefit from a fare structure that disadvantages some customers. This will depend on their ability to segment the market to their advantage.[18] However, the CIE note that in practice it is difficult for drivers and operators to choose which trips to service, particularly in a market where a significant share of trips are pre-booked.[19]

For this approach to work consumers would need to be educated about the different fare structures on offer by taxi networks. At present, all fare structures are the same within each licence area and consumers have the freedom to book or hail any taxi in the knowledge that the price paid will be the same for each taxi. However, in other industries consumers are required to educate themselves about the price charged by different firms before making their purchase. This would suggest if a de-regulated fare structure was adopted in Tasmania (or parts of) a cultural shift may be required for the industry and customer education required.

One complication with this approach is that for taxis hailed at a taxi rank, consumers tend to use the first available taxi i.e. the taxi at the front of the taxi zone. However, Regulation 57(5) of the Taxi Industry Regulations states, amongst other things, that a driver must not:

“(a) refuse to accept a hiring while the driver's taxi is in a taxi zone within the taxi area specified on the taxi licence under which the taxi is providing a taxi service; or

(f) inform a person that the person is required to hire the taxi standing in the foremost space within the taxi zone.”

That is, on a strict interpretation of the Taxi Industry Regulations, if a customer approached, for example, the third taxi in the rank, the driver of that taxi would be obligated to hire their taxi to that customer.

There may also be physical barriers at some ranks to moving specific taxis forward in line, such as at the airport. Furthermore, if consumers were to choose a taxi that is not first in line at a rank, this could cause tension amongst drivers and consumers at those ranks. To solve this problem, taxis hailed through a rank may need to charge based on the current fare structure relativities. Initial consultation with industry suggests that around 20 per cent of trips are hailed and thus would be subject to the current fare relativities with the 80 per cent booked based on the network operator’s desired fare structure. However, confusion may occur between the definition of what is a booked fare and what is a hailed fare.

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18 For example, if a network was able to capture a segment of the market and base their fares on the average trip for all of Hobart, their fare structure may result in higher revenue and costs to passengers then if it was based on a significantly different average trip from their new segmented market.

19 See The CIE (2012) “Setting taxi fares in Tasmania” Final Report, p.44.

Consultation

With respect to de-regulation of fares, the Regulator asked stakeholders:

- if they considered that a de-regulated fare structure would be appropriate for the taxi industry in Tasmania;
- if so in which parts of Tasmania should it be applied;
- whether a de-regulated fare structure be restricted to taxis that are booked, as opposed to those that are hailed through a taxi rank;
- what is an appropriate average trip in terms of distance travelled and waiting time for setting the maximum revenue that can be earned from the average trip;
- is there always a clear indication for consumers and taxi operators of what is a booked and a hailed taxi; and
- whether stakeholders saw this as an area of potential conflict?

Submissions

Industry stakeholders did not support de-regulation of the fare setting process. Stakeholders considered that de-regulation would cause unnecessary confusion for customers. Stakeholders consider that it would be difficult to distinguish between a booked and hailed taxi and consider that the public may not care. Furthermore, stakeholders consider that de-regulation may attract individuals to the industry that do not understand the real cost of operating a taxi. Stakeholders also suggested that these individuals often leave the industry after a short period of time which is disruptive for customers and may damage the public's perception of the industry.

DIER consider that there may be merit in de-regulation of some manner to improve the efficiency and responsiveness of the industry however are concerned that a weighted average price cap approach has the potential to disadvantage certain aspects of the market. DIER point to the example of WATs which predominantly have shorter trips and few operators that could lead to abuse of market power. DIER is concerned that a fare could be constructed that met the requirements of a weighted average price cap based on a longer notional trip but would effectively load the flagfall and disadvantage such customers. Ultimately whilst DIER consider that de-regulation has its merits a primary consideration should be that access to a taxi service is not significantly undermined for any sub group of passengers, whether they make journeys with particular characteristics or are eligible for subsidised travel.

Regulator's conclusion

Whilst the Regulator considers that there is merit in applying a less regulated structure to fares, the Regulator considers that there is at present insufficient information to adopt such an approach and to ensure consumers are adequately protected.

The Regulator considers that de-regulation via the use of a weighted average price cap may be an appropriate consideration in the future because the taxi industry understands its industry and client base best and may be in a better position to adjust fares to its benefit, subject to constraints placed on it by the Regulator to protect consumers and promote efficient outcomes. However, the Regulator notes that the taxi industry would prefer that fares remain fully regulated. Furthermore, the Regulator does not consider it has sufficient information on the average fare during different times of the day to adopt this approach either to ensure economic efficiency is promoted and consumers are adequately protected.

The Regulator notes the concerns of DIER in ensuring that customers are not disadvantaged. The Regulator notes that with any fare structure change, including de-regulation, some consumers would pay higher fares and would be worse off. For example, a higher flagfall would make shorter trips more expensive which adversely impacts some customers. However, a decision in the future on de-regulation would need to be a balance between improving overall economic efficiency and considering the impact on specific stakeholders. Furthermore, the Regulator notes that there are other mechanisms that can be used to compensate such parties if the government chooses to do so.

4.6 Price notification system

The recent Victorian Taxi Industry Inquiry (the Victorian Inquiry) proposed two alternative methods for setting fares.

The first involves the setting of maximum fares. Under this approach, a normal regulatory fare review occurs to determine fare increases. However, the difference is that taxi operators would have the flexibility to offer discounts to customers under this maximum fare amount. Under this approach, maximum fares would be recorded on the taximeter and drivers be allowed to provide discounts off the meter rate, as long as the meter is run as a protection for consumers. The advantage of this approach is that it allows participants in the market to adopt some competition with one another to the benefit of consumers. However, the disadvantage is that there is less certainty on the final fare. The Victorian Inquiry noted that “A large number of those opposing the change to maximum fares suggested that it would lead to unruly behaviour – especially at taxi ranks – and cause conflict between passengers and drivers about discounted fares. Others believed it would lead to disputes between operators and drivers in reconciling the meter with the fare box at the end of each shift.” [20]

The Regulator notes that a maximum fare system effectively already exists in Tasmania. As indicated in the terms of reference for this inquiry (see Appendix A), fares are regulated by a “standard fare” that cannot be exceeded. However, the actual charge for hiring can be less than the standard fare (as shown on the taximeter) at the driver’s discretion.

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[20] Taxi Service Commission (Victoria) (2012) “Customer First: Safety, Service, Choice – Taxi Industry Inquiry Final Report”, December 2012, pp.179-180.

The second method proposed by the Victorian Inquiry involves allowing taxi operators to set their own fares, however any fare change would need to be published with a public agency (a price notification system). The Victorian Inquiry notes that "tthe adoption of this system will put greater control in the hands of country operators and networks, allowing a tailoring of services and prices to the costs of running their business. Removal of such restrictions will also encourage greater flexibility, innovation and choice in taxi services."[21]

The Victorian Inquiry argues there is "a strong theoretical and practical basis for promoting more effective competition in the pre-booked commercial vehicle market. This market has very different characteristics from the rank and hail markets, with consumers having greater ability to choose between competing companies and hire car companies having a much greater reliance on repeat business. Competition can keep service standards higher in this market than in situations where the probability of repeat business is low (for example, the likelihood of catching the same taxi)."[22]

The Victorian Inquiry notes that a significant amount of regional Victoria taxi trips are based on pre-bookings. Thus the Victorian Inquiry recommended moving to a price notification system for regional Victoria, "following the implementation of price-based licensing policy in these areas."[23] This final step is designed to ensure sufficient competition emerges to compete with other operators in regional markets.

The Victorian Inquiry notes that the majority of taxi passenger trips in Melbourne are instigated through the rank and hail market where customers are unable to exercise choice. Given this, the Victorian Inquiry considers the regulation of maximum fares is appropriate for Melbourne at this stage.

Drawing paralells with the Tasmanian market, the Regulator understands that:

- around 80 per cent of passenger trips in Tasmania are pre-booked;
- there are four competing networks operating in Hobart, with only single networks or a co-op arrangement in other towns; and
- lease plates in Hobart and Launceston are significantly more valuable than in other areas suggesting licence supply restrictions may be inhibiting competition.

Given these factors above it would appear that:

- a price notification system may be appropriate for Hobart with a large pre-booked market and competition but given the current value of taxi plates it is unclear whether there is sufficient competition in the Hobart market;

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21 Ibid, p.13.

22 Ibid, p.91.

23 Ibid.p.54.

- a maximum fare system (the current approach) may be appropriate in Launceston due to insufficient competition in the Launceston market reflected by the single network and high taxi plate value; and
- a price notification system may be appropriate for other areas of Tasmania given a large pre-booked market and little value in taxi plates.

Whilst competition does not appear to be necessarily evident within the taxi industry in other areas of Tasmania, the fact that plate leases have negligible value (with some exceptions in those areas) suggest economic rent is not being earnt. If taxi operators did increase fares this may either lead to less demand with passengers seeking alternative transport methods or new players entering the market to erode any extra profits. That is, the current restriction on the number of licences being released may not be impacting on the achievement of competitive outcomes in other areas of Tasmania.

Consultation

The Regulator asked stakeholders if they believe that there are sufficient competitive forces in the Hobart and other (non Launceston) markets to consider adopting a price notification system?

Submissions

Stakeholders were not supportive of a fare notification system.

Regulator's conclusion

The Regulator does not recommend a fare notification system at this stage. However the Regulator considers that it may be worth reconsidering in the future if sufficient competitive forces exist in the market in which it is applied to.

4.7 Application of fares increases to fare components

If fare components are to remain regulated, the CIE outlines two options for applying fare increases to fare components.

The first is option is called the "average fare approach". This involves:

- specifying an average trip including distance travelled and waiting time;
- applying the fare increase to the current value of the average; and
- adjusting the fare components to ensure that the new value of the average trip is met through the new fare components.

This approach allows for flexibility in adjusting the fare component at each review if anecdotal evidence suggests that the current fare structure is sub-optimal.

The current approach is similar in nature to the above approach. However under the current approach each fare increase (percentage change) is applied equally to each fare component, which is similar to the current approach for most regulators in

Australia. The advantage of the current approach is that information is not required on the average trip. However, the disadvantage is that fare components are not able to be adjusted with confidence if the components are deemed to be unsuitable.

The second approach is called the “master fare schedule” approach. Under this approach fare components are adjusted by the proposed fare increase and then rounded. Subsequent fare increases are applied to the unrounded amount. The CIE notes that this approach is useful when dealing with small components in which fare increases must be rounded to 5 or 10 cent increments. For example, the CIE notes that if a booking fee was introduced of say one dollar, then a more than five per cent price increase would be required to achieve a 10 cent increment, which may never occur. However, since under a master fare schedule, fare increases are applied to previous unrounded amounts, over time this would occur. However, the CIE notes that the master fare schedule does not allow for a rebalancing of fares or the introduction of a new fare component.

The CIE recommends that the average fare approach be adopted if fare components remain regulated.

The Regulator asked stakeholders:

- for their views on the method for increasing regulated fare components; and
- if an average approach is adopted, what is an appropriate average trip in terms of distance travelled and waiting time?

Submissions

DIER considered that the master fare schedule may add complexity and that the fare setting process needs to be easily understood.

Another stakeholder considered that the average fare approach seemed appropriate and noted that a different adjustment to fares should apply in different licence areas given the different average trip lengths.

Stakeholders indicated, either through written submissions or orally, the following average trip distances:

- Hobart – 7 km;
- Launceston – 5 km; and
- Burnie – 4 km.

Regulator’s conclusion

The Regulator considers that the average fare approach is the more appropriate approach given stakeholders views and allowing for fare structural adjustments in the future.

4.8 Information requirements for consideration of a fare structure change

Throughout this section of the Final Report, the Regulator has outlined that at present it considers that there is insufficient information to assess and make changes to the current fare structure. The Regulator appreciates the submissions and data provided by selected stakeholders but the Regulator considers that this information is insufficient to support the making of changes for the industry across the different taxi areas. That said, the Regulator would like to outline the type of information that would be required in the future to consider whether to make fare structure changes. This information includes:

- evidence concerning the mismatch between demand and supply for different trips types (including waiting times), particularly for short suburban trips and night time trips; and
- details on the number of trips, average distance of those trips and revenue earned during different times of the day that can be broken down into any proposed tariff structure.

The first dot point would assist the Regulator in considering the efficiency of the current fare structure and what changes may need to be made to increase the number of trips to the benefit of consumers. For example, if sufficient evidence existed that indicated that short trips were not being met or had relatively long waiting times compared to long trips, this may suggest that the flagfall rate should be increased. However, this would be balanced against the social concerns and current social policy of the government.

The last dot point would assist to determine the average revenue earned from trips at different times of day and days of the week which could be used to inform how the magnitude of the fare structure should change. This could be used to make specific fare structure changes and to de-regulate fares and allow the taxi industry determine its own fare structure, subject to constraints constructed by the regulating body. Chapter 5 of the CIE's final report provided an example of how this may operate in practice.[24]

The Regulator notes that similar information was recently used by IPART in recommending a fare structure change for its current taxi fare review.[25] Specifically IPART used data from a passenger survey and an industry survey, including several years of anecdotal evidence, to inform its decision. A similar approach could be adopted in the future in Tasmania and/or data could be directly sourced from the smaller number of networks/operators that exist in Tasmania.

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[24] See The CIE (2012) "Setting taxi fares in Tasmania" Final Report, pp.48-49.

[25] IPART (2013) "2013 Review of taxi fares in NSW – draft report",p.41.

The Regulator considers that if this were to occur, it would be in a much better position at the next taxi fare methodology review to consider what adjustments to the fare structure should occur to the benefit of passengers and the industry.

5 COST WEIGHTS

This section discusses elements to include in taxi cost models to determine fare increases.

5.1 What should be included in the taxi cost model?

Selection of the items to be included in a cost model is critical if cost pressures faced by industry are to be accurately reflected. This is to ensure that:

- industry is able to recover its costs of doing business; and
- consumers are protected so that fare increases reflect only efficient cost increases.

Table 5.1 presents the cost items and weights contained within the current DIER taxi cost model.

Table 5.1: DIER current cost items and weights

Component	Weight 2011 Per cent
Vehicle lease cost	7.58
Vehicle equipment	4.19
Vehicle registration	2.10
Annual licence and inspection fee	1.68
Radio fees	10.97
Vehicle insurance	5.40
Workers compensation insurance	6.08
Personal Accident Insurance	1.82
Accreditation costs	0.53
Fuel	33.72
Vehicle maintenance labour and parts	24.02
Tyres – new	1.90

The DIER model excludes two cost items being:

- labour of operators and drivers; and
- taxi plate lease costs.

The Regulator understands that these items may have been historically excluded due to their circular relationship with fare increases. That is, a fare increase leads to:

- a similar increase in driver labour costs based on a 50:50 fare revenue sharing arrangement, without consideration of the value of driver labour; and
- an increase in plate lease values from the provision of a greater return to licence owners through higher revenue. As licences increase in value, plate lease costs to operators also rise which can lead to an increase in fares and further increases in the value of licences, hence a circularity.[26]

However, the CIE notes that exclusion of these major cost items means that other cost items have a much higher weight in the cost index than they otherwise would. For example, the weighting for fuel was around 34 per cent in 2011, compared to around 10 per cent observed in other jurisdictions.[27] This means that fuel price rises have a much larger impact on overall fare increases than would otherwise be the case if these items were accounted for in the model.

Whilst inclusion of labour and plate lease costs have the potential to create the circularity discussed above, this can be addressed separately through consideration of the method of indexing these items (see Sections 6.2 and 6.3 below).

The CIE recommends that all major cost items should be included in the model; however they do not necessarily need to be included separately. Items should be separated out when they move differently to general prices in the economy.

Given these considerations, the CIE suggests that all major costs should be included under the following categories:

- radio-room costs;
- vehicle costs (including fit-out);
- service, maintenance and repair;
- insurance;
- registration;
- operator labour;
- plate leases;
- driver labour; and
- fuel.

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26 This issue was discussed in detail during the recent Taxi Fare Review in NSW, see IPART (2012) "2012 Review of Taxi Fares in NSW – Final Report",pp.29-31.

27 The CIE (2012) "Setting taxi fares in Tasmania: Final Report", pp.23-24.

Consultation

The Regulator asked stakeholder if they considered if the proposed cost items are sufficiently representative of the operating costs for an average taxi in Tasmania.

Submissions

DIER expressed their concern that the inclusion of plate leases and driver wages creates a circularity in the determination of fares. However, DIER noted that the inclusion of licences costs with an appropriate deflator should address this concern.

All other stakeholders considered that the proposed cost items were reasonable.

Regulator's conclusion

The Regulator does not agree with DIER's view that exclusion of plate leases and driver's wages from the model removes any circularity in the determination of fares.

With regards to plate leases, at first glance one may consider that current prices do not recover plate lease costs as they are not included in DIER's current taxi cost index. However, whilst perhaps not directly included in the model that determines fare increases, the fact that licences have a positive value in Hobart, Launceston and other regions, is evidence that excessive profits are being earned that flow through to lease plate owners. Unless plate lease costs are included in the model and a zero or negative inflator applied, fares will increase by more than desired due to overweighting of other cost items as discussed above. This leads to continued inflation of licence values as a result of increases in taxi fares.

With regards to driver wages, exclusion from the model would mean that the model would effectively be an operator model that does not take into account driver costs. Thus the driver labour component of fares would be inflated by operator specific costs and not general wages pressure (which is discussed in more detail in Section 6.3).

The Regulator considers that the cost items are reasonable and are considered by taxi industry representatives to be representative of the costs facing the taxi industry.

5.2 How should the taxi cost model components be weighted?

Table 5.2 and Table 5.3 present the CIE's estimates of cost and cost weights for Hobart, Launceston and "Other" regions of Tasmania. These estimates are based on information provided to the CIE by DIER, industry through initial consultation, and through the CIE's own research. Not surprisingly, the inclusion of plate lease costs and operator and driver labour leads to a reduction in weights of other items, particularly for fuel and service and maintenance costs.

It is important to note that the following estimates aim to be representative of the costs of operating an average taxi in specific locations within Tasmania. They will not necessarily be the same as the actual cost of operating an individual taxi. Rather they aim to represent the average cost of operating a taxi. This takes into account the differences in specific taxis including different fuel arrangements (petrol, LPG and Hybrid's) and operator models ranging from the segmented market of licence owner-network-operator-driver to the complete owner-operator model with combinations in between.

Furthermore, whilst the total cost of operating a taxi in a specific area may vary, the cost weight of each cost component is what really matters for this method of setting fares. Table 5.3 therefore provides a representation of the percentage share of costs for a representative (i.e. average) taxi in each taxi region. As will be seen in the next section, cost increases are applied to the cost weights to determine the change in fares.

Table 5.2: Estimates of major annual cost items by area (including GST)

Cost	Cost shares		
	Hobart	**Launceston**	**Other**
	$/taxi	**$/taxi**	**$/taxi**
Radio room costs	7 200	7 281	11 880
Vehicle costs (including fit out)	4 806	4 718	4 372
Servicing, maintenance and repairs	7 657	7 034	5 200
Insurance	4 786	4 396	3 250
Registration	1 318	1 318	1 318
Operator labour	4 991	4 585	3 389
Plate leases	13 328	8 580	3 432
Driver labour[a]	60 356	52 857	32 441[b]
Fuel	16 271	14 947	11 050
Total	120 713	105 715	76 333

[a] Driver labour is the annual income earned by all drivers operating an average taxi in a specific taxi area. [b] Driver share is 50 per cent in Hobart and Launceston, 45 per cent in Burnie and 40 per cent in Devonport and Ulverstone.

Source: Appendix A of the CIE's final report (details of the assumptions used to calculate these estimates are also outlined in Appendix A of the CIE's final report).

Table 5.3: CIE proposed cost weights by area

Cost	Cost shares		
	Hobart	**Launceston**	**Other**
	Per cent	**Per cent**	**Per cent**
Radio room costs	6.0	6.9	15.6
Vehicle costs (including fit out)	4.0	4.5	5.7
Servicing, maintenance and repairs	6.3	6.7	6.8
Insurance	4.0	4.2	4.3
Registration	1.1	1.2	1.7
Operator labour	4.1	4.3	4.4
Plate leases	11.0	8.1	4.5
Driver labour	50.0	50.0	42.5[a]
Fuel	13.5	14.1	14.5
Total	100.0	100.0	100.0

Source: The CIE.

Consultation

The Regulator asked stakeholders whether:

- they believed that the proposed weights are representative of the average taxi operating in each taxi area; and
- they had different information they wish to submit?

Submissions

Stakeholders considered the proposed cost weights to be reasonable. Some additional data was provided by Taxis Combined Launceston on plate lease costs which has been used to slightly adjust Table 5.3.

Regulator's conclusion

The Regulator recommends that the proposed cost weights be adopted for future fare methodology reviews.

6 INDEXATION, PLATE LEASES AND PRODUCTIVITY ADJUSTMENTS

This section discusses specific inflators to use in determining changes to the cost weights discussed in Section 5 of this paper that will, ultimately, determine the change in overall fares.

6.1 Indexation

Once the cost weights have been determined, these weights are multiplied by cost inflators/deflators to determine the weighted average cost increase for an average taxi.

The CIE notes that there are two broad methods for determining inflators:

- independent publicly available estimates including ABS Consumer Price Index measures, official interest rate data and data collated on fuel prices; and
- quotes from industry (for example, obtaining a quote from networks on their network fees each year).

The disadvantage of public estimates is that they may not align well to the cost item being measured.

However, the disadvantages of quotes from industry are more numerous including not necessarily representing prices paid (full price versus discounts) and may be subject to gaming by industry.

The CIE recommends, on balance, the use of independent publicly available estimates. The Regulator understands that most cost index based approaches used by Regulators are moving from industry quotes to independent public estimates, thus the use of this approach would be consistent with current regulatory trends.

Table 6.1 outlines the inflators proposed by the CIE for each cost item it suggests should be in the index. These inflators have been chosen as most closely representative of each cost weight. Further details can be found in Chapter 9 of the CIE's final report.

Table 6.1: The CIE's proposed inflators

Cost item	Inflator
Radio room costs	ABS CPI, Communications for Hobart
Vehicle costs (including fit out)	ABS CPI Motor Vehicles Hobart and RBA small business indicator rate for variable loans
Servicing, maintenance and repairs	ABS Consumer Price Index for maintenance and repair, Hobart
Insurance	ABS CPI, Insurance for Hobart
Registration	Government regulated fees[28]
Operator labour	ABS Wage Price Index for Tasmania (Public and Private)
Plate leases	0 per cent or negative growth, see Section 6.2
Driver labour	ABS Wage Price Index for Tasmania (Public and Private)
Fuel	Average annual percentage change in fuel costs for Hobart from Fueltrac

Source: The CIE.

Consultation

The Regulator asked stakeholders if:

- they agree with the use of independent publicly available estimates for inflators; and
- if they agree with the CIE's suggested inflators.

Submissions

All stakeholders agreed with the use of independent publicly available estimates for inflators.

Some stakeholders expressed concerns about the use of the ABS CPI Communications Hobart inflator for radio room costs. One stakeholder considered that this may be predominantly labour costs and suggested that the wage price index may be more appropriate. DIER noted that provision of radio room services requires a range of inputs including land and buildings, telephone, equipments and services, labour and specialist information technology. DIER considers that the use of a broader inflator may be appropriate to capture these additional elements.

With respect to the other proposed inflators, apart from plate leases and labour which are discussed below, all stakeholders considered these to be reasonable.

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28 The change in cost for this item will be observed based on the regulated fees set by DIER and the MAIB. See http://www.transport.tas.gov.au/fees/calculation_of_fees_-_class_a_vehicles and http://www.maib.com.au/premiums.

Regulator's conclusion

The Regulator recommends the use of independent publicly available estimates for inflators.

With respect to radio room costs, the Regulator considered the advice in the CIE's final report. The CIE note that over the past ten years, the Communications sub-component of the Hobart CPI has increased by around 14 per cent, yet DIER has inflated radio room fees in the taxi cost model by around 33 per cent over the same period based on quotes from industry sources. The CIE consider that while this suggests that the communications sub-component of the CPI may not accurately reflect changes in radio room costs, the CIE nevertheless consider that communications is likely to be the most appropriate inflator. It captures broad trends in communications pricing such as mobile phones and would reflect changes in the price of all inputs, such as labour, land, capital and intermediate inputs, as well as changes in productivity from technological innovation and other sources. The CIE note that one reason why radio room prices may have increased at a faster rate than broader communications prices is that there is less competition and therefore less innovation. In the period ahead there would seem to be significant scope for technological innovation in the provision of radio room services from smart phone apps etc.[29]

Based on this advice, the Regulator considers the use of the ABS CPI Communications Hobart inflator for radio room costs to be reasonable.

Furthermore, the Regulator considers that all remaining inflators to be reasonable as outlined in Table 6.1.

6.2 Plate lease costs

Taxi plate lease costs are a real cost faced by operators, and a significant one for operators of standard taxis. Plate lease costs constitute 11 per cent of the costs of providing taxi services in Hobart.

However, their inclusion in the taxi cost model is problematic as outlined in Section 5.1. The value of a taxi licence reflects, at least in part, the expected earnings from fares. As fares go up, so does the value of a taxi licence and the associated lease. If the change in plate lease cost is used to set the fares, there is a degree of circularity that may serve to accelerate fare increases.[30]

29 See The CIE (2012) "Setting taxi fares in Tasmania: Final Report", pp.71-72.

30 At first glance one may consider that current prices do not recover plate lease costs as they are not included in the current taxi cost index of DIER. However, whilst perhaps not directly included in the model that determines fare increases, the fact that plates leases have a positive value in Hobart, Launceston and Burnie, is evidence that excessive profits are being earned that flow through to plate owners. Chart 9.4 of The CIE draft report shows the cost of licence plate sales in recent years on the secondary market.

Furthermore, the plate lease cost is not an efficient economic cost. Rather, the plate lease cost represents the financial value of plate leases that arises due to restrictions on the supply of lease plates, known as an “economic rent”. If the market for lease plates was competitive and there were no restrictions on supply, then new entrants would enter the market thereby eroding the value of the taxi plate and, in turn, the plate lease cost. In other industries, regulators keep a check on potential economic rents by only allowing for the inclusion of efficient economic costs when determining prices.

The difficulty in the taxi industry is that this economic rent has largely been created by the long established policies of government to restrict the supply of taxi plate licences. This has created a market for individuals to purchase and own taxi licences as an investment but not operate taxis themselves. As with any investment, investors expect a rate of return on that investment (including funds to repay loans used to fund that investment), which is provided through the lease plate financial cost charged to operators. This cost however is funded by consumers through higher fares.

There are two possible ways to deal with this problem through the fare setting methodology.

The first is to assign zero growth to the cost weight for plate leases. This has the effect of removing any circularity between the value of plate leases and fare increases and, all other things being equal, maintaining the current value of lease plates. This is because fare increases will be based on increases in physical costs excluding the plate lease costs. Hence any fare increase would be used to pay for this increase in cost with no additional funds available for taxi plate owners. Given this, both the return to taxi plate owners and the value of taxi plates would remain unchanged, all other things being equal. Furthermore, consumers would only pay for increases in other costs and would pay no more than what they are currently paying for plate lease costs. This approach was recently used by the NSW regulator IPART[31] and is used by the Western Australian government.[32]

The second is to assign negative growth to the cost weight for plate leases. This would ensure that the contribution of plate lease costs to fares would fall over time with fares moving toward efficient economic cost. Furthermore, it would reduce the residual amount of funds (above other costs) available to be passed to taxi plate owners and, in turn, the value of taxi plates.

The solution to this problem would appear to depend on how much weight is placed on the respective interests of taxi plate owners and consumers. This was the subject of the discussion in Section 3.

Another way of dealing with this issue is to vary the rate at which new licences are released and taken up. An increase in the number of licences released and taken up

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31 IPART (2012) “Review of taxi fares in NSW, Final report”.

32 See PricewaterhouseCoopers (2011) “Update of the 2011 taxi fare increase, prepared for the Western Australian Department of Transport”.

will increase the supply of taxis on the road for consumers. This will reduce the number of fares available per taxi and thus the revenue and return for plate lease owners per taxi.

The Regulator notes that DIER is currently undertaking a review of licence releases in conjunction with the taxi fare review. Whilst the Regulator has been instructed to conduct the taxi fare inquiry in isolation to the licence review, the Regulator notes that the outcomes of DIER's licence review will impact on the value of taxi plates in the future. That is, if more licence plates are released, relative to the increase in demand for taxi services, then the value of taxi plates will fall. This fall in value would be reflected in the value of the cost weight for plate leases when the weights are next reviewed. Appendix B outlines how IPART and the Victorian Taxi Industry Inquiry are considering the dynamics between future licence releases and the treatment of plate lease in fare modelling.

Given the dynamics between licence releases and fares, the CIE's final report recommends a deflator be applied to plate lease costs that reflect the number of licences being released. That is, a higher deflator is applied if fewer licences are released and taken up or a lower deflator is adopted if more licences are being released and taken up. The CIE recommends that the deflator should be five per cent per year if licence releases remain at the same rate.

Ultimately, this is a matter of government policy; however the Regulator wishes to consult with stakeholders to inform the debate.

Consultation

With respect to plate lease costs the Regulator asked stakeholders for:

- their views on the option of assigning zero growth to the cost weight for plate leases;
- their views on the option of assigning negative growth to the cost weight for plate leases;
- in the event that a negative growth factor is applied to the cost weight for plate leases, what are their views on the value of the inflator/deflator to be applied; and
- when considering this issue should the Regulator consider the interests of taxi plate owners, consumers or a balance of both?

Submissions

Stakeholder views were mixed with respect to this item.

DIER outlined in its submission that deflation of plate lease costs should be considered. DIER argue that Tasmania has a legislated program of allowing additional plates to be offered for sale each year which is intended to gradually decrease scarcity value over time. DIER also outlined that the reserve price offered for these plates is fixed at a legislative value which effectively declines in real terms over time, thus by extension DIER consider that the plate lease figure adopted in the model should also decline. In this respect DIER consider that the interests of consumers should be the primary concern. Furthermore, DIER consider that the deflator should be gradual so as to not to create immediate disadvantage for existing industry members and it should be clearly specified in advance to ensure it is not subject to lobbying or other influence.

Yellow Cabs in Hobart and Taxis Combined in Launceston do not support the use of a negative inflator for perpetual taxi licences. They consider it reasonable for a perpetual licence owner to continue to earn a positive and growing return on their investment. That said, both indicated that should adjustments be made through fares or licences releases that impacted on the value of a Perpetual Taxi Licence and also plate lease costs, they consider that the Government should compensate the Perpetual Taxi Licence owner.

Regulator’s conclusion

The Regulator acknowledges the competing views on this issue and is well aware of the implications of its recommendations on this issue. Considering both sides of the debate, in the short term the Regulator recommends that a zero per cent inflator be applied. Adopting this method would ensure that any increase in the value of licences would not be passed through fares to consumers. Furthermore, fare regulation would not directly impact the nominal value of licences (in real terms this approach will lead to a decline in real value because additional revenue is not provided to allow for an increase in the nominal value of licences). Indeed this approach would appear to be consistent with the current approach of the Government. That is, DIER has outlined in its submission that the reserve price offered for these plates is fixed at a legislative value which effectively declines in real terms over time.

This issue is difficult to resolve in the absence of a clear policy position from Government on the issue of the value of licences. Whilst the Regulator appreciates DIER’s position, to date, there does not seem to have been any apparent correlation between the policies relating to fare regulation and licence releases and DIER’s position with respect to consumers. Specifically, as outlined in Section 3, Figure 3.1, whilst the Government’s current policies may have stemmed the increase in the value of perpetual licences in recent years it has not led to a decline in those values.

Given this, and not knowing what the Government’s policy will be following the completion of DIER’s current licence release review, the Regulator considers it prudent to apply a zero per cent inflator until further direction is provided by government.

6.3 Driver labour costs

As shown in Section 5.1, driver labour costs are included in the model to reflect the current revenue sharing arrangement between drivers and operators. That is, the cost weight for drivers is 50 per cent in Hobart and Launceston, reflecting the fact that drivers currently take home 50 per cent of the fare revenue for those taxi areas.

This revenue split is an arrangement within the industry and is not subject to regulation.

The CIE note that "the current cost index presumes that the cost sharing arrangements will continue and that only measures operator costs. This effectively says that if there is a 10 per cent increase in operator costs, a 10 per cent increase in fares is required to cover operator costs, with drivers also benefitting." [33]

The CIE also notes that "We consider that it is not the role of the regulator to use fares to influence the share of revenues that goes to drivers, operators and other relevant services providers." [34]

Based on this logic, an independent measure is required to inflate labour costs in the model. The CIE has recommended that driver and operator labour costs be inflated by the increase in the ABS Wage Price Index for Tasmania (Public and Private). This has the effect of allowing for wages growth in the model to be similar to the Tasmanian average.

In addition, it removes the mechanical circularity between the total level of the Cost Index and weight to be applied to driver labour costs. As discussed above, under the current model any increase in operator costs also leads to a commensurate increase in fares and effectively driver costs, through the revenue sharing arrangement. If this were maintained in the new model through maintaining the 50 per cent weight, then further increases in operator costs would lead to increases in driver costs and providing a continued double impact on fares. The only difference is that the impact would be more explicitly visible.

With more regular reviews and the inclusion of lease plate costs, in future any negative impacts from fuel price and plate lease cost falls will lead to a double negative impact on fares, through the link to drivers costs. This is because, to maintain the 50 per cent weight, a deflator (or reduced level of inflator) would need to be applied to the driver labour cost weight. Similar to above this impact would occur independent of general wages of workers. Using the independent measure of WPI removes this circularity.

The regulatory decision will also be independent of any driver operator revenue sharing arranging. These arrangements can continue to be negotiated within the industry. From the initial consultation it is understood that some operators are beginning to pass some of the costs onto drivers such as costs for workers compensation and cleaning. In addition, the driver revenue sharing arrangement is less in Burnie, Ulverstone and Devonport. Should these arrangements between regulatory periods change, the driver labour cost weights can be adjusted at the next cost weight review.

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[33] The CIE (2012) "Setting taxi fares in Tasmania: Final Report", p.72.

[34] Ibid p.72.

Consultation

With respect to labour costs, the Regulator asked stakeholders for their opinion:

- should labour costs be inflated by the ABS Wage Price Index for Tasmania (Public and Private); and
- do stakeholders have a view on an alternative measure?

Submissions

Stakeholders were generally supportive of including labour costs in the model including the proposed inflation method. One stakeholder suggested that the use of Average Weekly Ordinary Time Earnings (AWOTE) may be another appropriate measure.

Regulator's conclusion

The Regulator considers the CIE's recommendation to adopt the ABS Wage Price Index for Tasmania (Public and Private) to be the most appropriate. The Regulator understands that Tasmanian AWOTE is based on a relatively small sample size and thus can be subject to large and unrepresentative fluctuations.

6.4 Productivity

The CIE also recommends including a productivity adjustment to encourage the taxi industry to be more efficient over time.

The CIE notes that the Cost Index approach is designed to measure a change in the cost of providing taxi services, based on changes in the price of inputs (including labour, capital and intermediate inputs). A Cost Index therefore assumes a fixed quantity of inputs, thus if the taxi industry improves productivity performance the Cost Index will overstate actual cost increases faced by the industry. Hence, applying a productivity adjustment to the cost increase measured by the Cost Index helps to simulate the outcomes that would be expected in an unregulated market with open entry. [35]

The CIE notes that a productivity adjustment:

- provides a signal to market participants to improve performance; and
- ensure that some of the benefits of productivity gains are passed onto consumers.

[35] Ibid p.77.

Furthermore, the CIE notes that productivity improvements within the taxi industry should occur through:

- more efficient use of labour and capital – this could be through more passengers per shift through better technology to link drivers to passengers or more demand, relative to the supply of taxis; or
- more efficient use of intermediate inputs – this could include use of more efficient use of fuel, either through less running without a passenger or use of more fuel efficient vehicles. [36]

A productivity adjustment is currently applied when calculating the taxi fare increases in NSW and Victoria.

In terms of the practicalities of applying a productivity adjustment, the CIE, in their final report, consider the measure of productivity adjustment to use, the length of time for calculating this measure and what to apply it to specifically. The CIE recommends that:

- a productivity adjustment should be applied to the cost increase estimated by the Cost Index;
- the productivity adjustment should be based on average economy wide productivity growth over the past ten years;
- if this is less than zero, that no productivity adjustment should be applied; and
- the productivity adjustment should be based on either a gross output or gross value-added measures of multi-factor productivity (and appropriately applied as outlined in the CIE's final report).[37]

With respect to productivity, the Regulator asked stakeholders for their opinion:

- about applying a productivity adjustment to the outcomes of the taxi cost index;
- if stakeholders have any views concerning the mechanics of the productivity adjustment recommended by the CIE above; and
- if stakeholders have evidence to suggest that productivity growth within the taxi industry is faster or slower than the economy wide average?

Submissions

Stakeholders considered it reasonable to apply a productivity adjustment to the cost index in determining fares.

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[36] Ibid p.77.

[37] See Ibid p.79.

With regards to the level of productivity adjustment to apply, one stakeholder considered that the industry may experience slower productivity growth than the economy wide average. DIER on the other hand considered that perhaps the taxi industry in Tasmania could experience faster productivity growth as they contend it is less regulated than taxi industries in other jurisdictions. DIER point to technology such as smart phone applications which allow passengers to locate taxis more efficiently. DIER considers that there is less regulatory restriction in Tasmania compared to other states to adopt this technology.

Regulator's conclusion

The Regulator recommends that the CIE's proposal for a productivity adjustment be adopted. Specifically, the Regulator recommends the use of the gross output measure of multi-factor productivity applied to the entire cost model due to its simplicity in application (over the gross value added method), average over a 10 year period. The Regulator considers that there is insufficient evidence to suggest whether the Tasmanian taxi industry could achieve more or less productivity growth compared to the economy wide average.

7 FARE SETTING PROCESS

The CIE makes a number of recommendations aimed at improving the regulatory process. These recommendations acknowledge the current lack of a clear, transparent and regular process for setting fares in Tasmania. These are outlined below.

7.1 Initiation of reviews

The CIE notes that, at present, fare reviews are initiated by industry, largely due to concerns over rising costs, particularly fuel costs. Through the initial consultation, stakeholders noted that without a defined and regular process the industry may be experiencing higher costs for some time until a fare increase is approved.

The CIE notes the following three options for initiating future fare reviews:

- maintain the current process of industry approaching the government when cost rises are significant;
- a price setting agency undertake periodic reviews (e.g. annually); or
- an industry group submits a proposal for a specific price increase, either at regular intervals or on an ad hoc basis.

Given that there is no single organisation representing the taxi industry in Tasmania and interstate, periodic reviews initiated by government are the common approach used in other jurisdictions to set fares in the taxi industry. Individuals / organisations within the industry are generally free to provide submissions as part of the review process.

Consultation

The Regulator asked stakeholders if they agreed with the CIE's recommendation that reviews should be initiated periodically by a price setting agency.

Submissions

All stakeholders indicated a preference for periodic reviews to occur.

Regulator's conclusion

The Regulator recommends that a price setting agency undertake periodic reviews that provide certainty to all stakeholders to when fares will be reviewed and adjusted.

7.2 Length of regulatory period

The appropriate length of a regulatory period may depend on the nature of the industry that is being regulated. That is:

- a longer regulatory period creates a predictable operating environment for industry and increases price certainty for consumers. Longer regulatory periods create greater incentives for efficiency given that the regulated business is able to retain any achieved cost savings until the following review period (above any productivity adjustments imposed by the Regulator); or

- a shorter regulatory period may be favoured where this can better balance risks between regulated businesses and consumers. This may be necessary if data used to implement the regulatory review is variable and subject to large forecasting errors.

The CIE notes that, under its recommendations, prices would be adjusted annually through the Taxi Cost Index which may better reflect interim costs when compared to other industries.[38] This means that there would be less risk of mismatches with industry cost and fare changes.

Given this, the CIE recommends a major review every four years in which the cost weights are re-examined with fares adjusted mechanically on an annual basis by the cost index.

Consultation

The Regulator asked stakeholders if they agreed with the CIE's recommendation that a major review should be conducted every four years with fares adjusted mechanically by the cost index each year?

Submissions

All stakeholders supported the proposal to adjust fares mechanically by the cost index each year. Furthermore, all stakeholders agreed with undertaking major reviews every four years with the exception of DIER.

In its submission, DIER, note that the taxi industry has been subject to slow but continual progress through multiple rounds of consultation. DIER is concerned about the impact of "consultation fatigue". Given this, DIER considers that five year intervals for major reviews may be more appropriate, similar to the regulation of Metro Tasmania.

Regulator's conclusion

The Regulator recommends adopting the CIE's recommendations as they are with major reviews every four years and fares adjusted annually by the cost index. Whilst the Regulator appreciates DIER's concerns about consultation fatigue for the

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[38] The CIE (2012) "Setting taxi fares in Tasmania: Final Report", p.92.

industry, the Regulator considers if the recommended process is adopted, this would be a substantial change from the current process. Given this, the Regulator considers a shorter-time frame may be more appropriate to consider the impact of the changed process earlier and to make any necessary adjustments as required. The Regulator also notes that of the submissions it received, industry participants appeared comfortable with the proposed process and timeframe.

7.3 Triggers and pass throughs

Within the suggested four year regulatory period there may be major changes in costs that would suggest that prices should be revisited. These changes could lead to a new major review or pass-through of additional costs into prices without considering other items.

The Australian Energy Regulator (AER) has proposed circumstances in which an event should lead to a reopening of the regulatory process.[39] Under these conditions, prices would be reconsidered where:

- the regulated entity is materially affected by the event;
- the event was beyond the regulated entity's control;
- the event was not contemplated at the time the revenue control decision was made; and
- the benefits of revoking the control decision outweigh the detriment to the regulated entity's customers from revoking the control decision.

That said, the CIE notes that "There is potential for trigger mechanisms to introduce bias into regulatory decisions, given that a regulatory process is usually only re-opened at the request of industry".[40] To some extent, this may have been occurring within Tasmania over the past 10 years with fare increases occurring when fuel prices rise, there hasn't been any corresponding fare decreases when fuel prices have fallen.

The CIE note that these impacts "...can be minimised where the regulator can monitor events and by imposing a materiality threshold on events."[41]

There are three potential changes that may lead to a pass through or an interim review of the taxi cost model. These include:

- substantial changes in fuel costs — because these would be incorporated into the cost index with a time lag there may be a need for interim price changes. The NSW pricing regulator, IPART, reviews fuel costs at six month intervals;

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39 Australian Energy Regulator (2012) "Pass-throughs and revenue-cap re-openers: Position paper" December.

40 Ibid.

41 The CIE (2012) "Setting taxi fares in Tasmania: Final Report", p.92.

- changes in regulatory arrangements, such as vehicle specifications; and
- changes in taxation arrangements, such as a change in the level of GST. In most instances, this type of change is known and can be incorporated into earlier pricing determinations. This would involve a straight forward adjustment to the cost index.[42]

The CIE has recommended that major costs resulting in a greater than a one per cent change in total costs that are not captured by the taxi cost index (such as regulatory and tax changes) should be passed through to taxi fares. The Regulator understands that changing meters to reflect changes in fares is a relatively costly exercise. Given this, a one per cent threshold may be a material threshold where the taxi industry may receive the benefits of a fare increase relative to the cost of changing meters within review periods.

The CIE considers that the administrative costs of reviewing fuel costs at six monthly intervals would outweigh the benefits of doing so in Tasmania. Under this approach, whilst industry may be at risk of facing fuel price spikes between fare increases, industry would also receive the benefits if fuel prices fall below the specified level within the taxi cost index. Furthermore, fuel prices and prices of other items within the cost index, would be adjusted on an annual basis which would be more regular than the current process.

However, through the initial consultation it is understood that some stakeholders may welcome more regular reviews of fuel prices. If fuel prices were monitored six-monthly, a threshold would need to be considered for changing fares. IPART currently monitors LPG fuel costs on a six-monthly basis and makes a recommendation on new maximum fares when LPG costs have changed by more than 20 per cent.[43] Following this review, fares may rise or fall depending on the outcome of the fuel price review.

Consultation

With regards to triggers and pass-throughs, the Regulator consulted on the following matters:

- do stakeholders agree with the CIE's recommendations on triggers and pass throughs;
- what is a material threshold for allowing for cost pass throughs during review periods, considering the cost of changing meters;
- would stakeholders like to see six monthly reviews of fuel prices; and
- if so, considering that the fuel weight in the proposed cost index is around 12 per cent (which means that fuel price rises contribution to overall cost

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[42] Ibid p.93.

[43] IPART (2012) "2012 Review of taxi fares in NSW – Final report". June 2012.

increases is 12 per cent multiplied by the fuel price rise) what would be the threshold for a material change to fuel prices?

Submissions

All stakeholders supported the CIE's recommendations with respect to triggers and pass throughs.

Furthermore, all stakeholders supported six-monthly reviews of fuel prices.

With respect to the quantum of a change in fuel prices that would be considered material, stakeholders' comments ranged from one per cent to three per cent.

Regulator's conclusion

The Regulator agrees with the CIE's recommendations for triggers and pass-throughs but also considers that six-monthly monitoring of fuel prices is warranted. The Regulator considers that fuel cost changes should only occur for extraordinary events. Given this, the Regulator considers that fuel cost changes that lead to an overall cost change of more than three per cent should be considered for fare adjustments at six-monthly fuel reviews. If this were to occur, the Regulator considers that the movement in other cost items should also be taken into account in deciding whether to pass cost increases through to fares or to conduct an interim review of costs.

7.4 Consultation during reviews

The CIE's final report contains recommendations with respect to the method and timing of consultation during any future taxi fare setting reviews. In particular, the CIE notes that the consultation process should be proportionate to the issues being addressed.

The CIE therefore recommends undertaking detailed consultation at each major review (every four years) following the consultation models adopted in NSW and Victoria. This involves the following steps:

- an issues paper is released informing stakeholders of the release of the terms of reference, the proposed approach to the review and timelines;
- call for written submissions on the issues paper;
- the holding of a public forum with key stakeholders;
- release of a draft report that summarises the findings and responds to submissions on the issues paper and issues raised at the public forum;
- call for written submissions on the draft report; and
- release of a final report considering all relevant data and submissions.

Additionally, given that the CIE propose the use of the mechanical formula to determine fare increases annually within the regulatory period, it does not recommend consultation be undertaken as part of the annual reset process. Given that fares would be set through the cost index and observed inflators, there would be limited scope for stakeholders and the Regulator to makes changes between major reviews. This is consistent with the Regulator's current approach for annual resets between major reviews for other regulated industries.

Consultation

With respect to consultation the Regulated asked stakeholders:

- how much consultation would stakeholders like during major reviews;
- do stakeholders agree with the CIE's recommendations on consultation;
- do stakeholders believe a shortened process, such as one round of written submission and a draft and final report would be sufficient;
- do stakeholders want a public hearing; and
- do stakeholders agree that consultation is unnecessary for annual reviews using the mechanical formula?

Submissions

The majority of stakeholders considered that two rounds of consultation during major reviews is appropriate but did not see public hearings as necessary.

DIER indicated in its submission that consultation can be problematical because the taxi industry in Tasmania does not have a single representative body and the industry does not respond readily to calls for submission.

All stakeholders considered that consultation is not required for annual reviews.

Regulator's conclusion

Based on the submissions provided, the Regulator recommends that:

- up to two rounds of consultation be undertaken during major reviews;
- public hearings not be held; and
- consultation not be undertaken during annual reviews when the mechanical formula is updated.

7.5 Agency undertaking the review

Taxi fare setting can be undertaken by a government department or by an independent pricing regulator. In NSW and Victoria, independent pricing regulators have historically undertaken the fare setting reviews and have provided recommendations to government. In other states and territories, including Tasmania, the task has been undertaken by the Department of Transport (DIER in Tasmania's case) or corresponding agency.

The CIE note that it considers “that it is more important that the processes are transparent and allow for open consultation than that the review be done by a particular agency. However, the independent regulator may be better able to ensure that reviews occur in this way, because this is the common structure used for other pricing reviews. The transparency of arrangements used by government departments has traditionally been far lower than those used by independent regulators.”

Consultation

The Regulator asked stakeholders who should undertake periodic reviews of taxi fare setting and indexation?

Submissions

All stakeholders considered that the Regulator should undertake the major four-yearly reviews and the majority of stakeholders considered the Regulator should also undertake the annual reviews. DIER considered that there is merit in the Regulator undertaking the major reviews but did not consider it necessary to have an independent body such as the Regulator conduct the annual indexation.

Regulator’s conclusion

The Regulator notes that there appears to be support for an independent body undertaking all future taxi fare reviews, including major four-yearly reviews, annual indexation and six-monthly fuel monitoring.

The Regulator appreciates DIER’s view that annual indexation may not necessarily need to be undertaken by the Regulator. However, the Regulator sees the value in all reviews remaining with the one body to ensure continuity of process and consolidation of corporate knowledge.

The Regulator considers that transparency and certainty with the fare setting process is crucial. The Regulator’s processes are designed specifically for price regulation, including:

- requirements to undertake reviews as outlined in legislation;
- undertake consultation on those reviews; and
- provide public reports.

The Regulator considers that there is some merit in an independent body undertaking future reviews consistent with the current and past practice in NSW and Victoria.

7.6 Funding future reviews

Conducting any regulatory process naturally costs money to employ staff, engage consultants and to cover overheads and the like. The Regulator understands that, given that taxi fare reviews have been infrequent, funds required to undertake reviews of the nature proposed in this Consultation Paper may not necessarily be available or easily obtainable.

The Regulator understands that DIER undertakes fare reviews and associated processes as required, using its ongoing core budget allocation. The Regulator also understands that, in order to fund this inaugural fares Inquiry by the Regulator, DIER has collected a portion of the annual licence fees that have been levied since 2009. The licence fees have been set specifically to recover a range of costs, including for this Inquiry.

The Regulator is currently funded directly by the industries that it regulates. That is, for each regulatory review and process that the Regulator undertakes, it is funded directly by the entities within that industry. Most closely related to the taxi industry is perhaps the Regulator's regulation of Metro and MAIB. The Regulator invoices these entities once every four or five years at the completion of its price review. These entities are then permitted to recover this cost through the prices they charge consumers.

The practice applied to fund this inaugural Inquiry by the Regulator is consistent with the approach described above. Therefore, one option is to for DIER to simply continue to levy annual licence charges to raise revenue directly from the taxi industry to fund the reviews. The annual fee would be adjusted based on the expected cost of the next review, and other factors such as the number of additional licences issued. This cost would then be included within the proposed taxi cost index to ensure that the cost is directly passed onto taxi passengers, as the Regulator understands has occurred since 2009 with DIER's own cost model.

Consultation

The Regulator asked stakeholder for their views on subject to the adoption of the review process recommended by the CIE, in funding future reviews, are stakeholders supportive of licence fees continuing to be levied (and potentially increased, as required) increased to fund those reviews?

Submissions

All stakeholders were comfortable with future reviews being funded through licence fee increases if necessary.

Regulator's conclusion

The Regulator recommends that the cost of all future reviews be funded through licence fees.

8 APPENDIX A: TERMS OF REFERENCE

Economic Regulator Act 2009

TAXI FARE METHODOLOGY INQUIRY

TERMS OF REFERENCE

The Tasmanian Economic Regulator is to conduct an inquiry under Part 5 of the *Economic Regulator Act 2009* and report to the Transport Commission on appropriate methodologies for setting and indexing taxi fares in Tasmania.

Background

The Transport Commission administers the *Taxi and Luxury Hire Car Industries Act 2008*. The Taxi and Luxury Hire Car Industries Act and the *Taxi Industry Regulations 2008* were developed after a comprehensive review of the previous legislation, which was undertaken during 2006 and 2007. Changes to the Taxi and Luxury Hire Car Industries Act made as a result include:

a) clarification of the distinction between taxis and luxury hire cars;

b) improved arrangements for wheelchair-accessible taxis (WATs), including increased availability of WAT licences; and

c) cessation of the issue of perpetual taxi licences and introduction of new owner-operator taxi licences.

Under the Taxi and Luxury Hire Car Industries Act[44], a taxi is a public passenger vehicle that is operating under a licence that authorises the vehicle to be hired on demand within, to or from the taxi area to which the licence relates:

a) from a taxi zone (rank);

b) by being hailed; or

c) by being booked or ordered.

Tasmania is divided into 24 taxi areas, which roughly correspond with the municipal boundaries. The Hobart taxi area comprises the majority of the Greater Hobart area and the Launceston taxi area overlaps with neighbouring taxi areas.

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[44] In late 2011 Parliament passed amendments to the Taxi and Luxury Hire Car Industries Act that, among other things, change the definition of a taxi. The amendments are intended to commence in 2013 and will not have a bearing on this Inquiry.

There are four different types of taxi licences:

A perpetual taxi licence – which can be bought or sold on the open market and is owned by the licencee in perpetuity or until the licence is sold to another licencee. It can be leased or assigned. It cannot be cancelled. No new perpetual taxi licences are available from the Transport Commission.

An owner-operator taxi licence – which can only be held by the licencee and must be operated by the licencee. It can only be held by a natural person who is accredited to operate a taxi service and it cannot be leased or assigned. It can only be sold to a person who meets the criteria for the issue of a licence. It can be cancelled without compensation under certain circumstances, such as if the licence has been leased. The Commission must make available for issue limited numbers of new owner-operator licences each year in each taxi area. There is no requirement for these licences to be taken up.

A wheelchair-accessible taxi (WAT) licence – which operates with a wheelchair-accessible vehicle, but may also carry non wheelchair-reliant passengers. WATs have a higher fare structure when carrying wheelchair-reliant passengers, which is offset by the provision of higher taxi fare subsidies to these passengers. The WAT fare and subsidy arrangements are currently under review. WAT licences are available on application from the Transport Commission provided the applicant is accredited to provide a taxi service and has a vehicle that is compliant with the *Disability Standards for Accessible Public Transport 2002* and the requirements of the Act.

A temporary taxi licence – which may be issued to an accredited operator of a taxi service for a limited period. It has the same effect as an owner-operator taxi licence for the period it is in force and cannot be bought or sold on the open market.

Taxis must be fitted with an operating taxi roof sign and taximeter. Taxis operating in taxi areas close to metropolitan centres are required to be fitted with a security camera system.

Fares are regulated by a "standard fare" that cannot be exceeded. However, the actual charge for a hiring can be less than the standard fare (as shown on the taximeter) at the driver’s discretion.

Current fare setting arrangements

A formal process does not currently exist for reviewing taxi fares in Tasmania. The Department of Infrastructure, Energy and Resources (DIER) maintains a taxi cost model, which was developed by DIER in conjunction with the taxi industry and has been used for a number of years. DIER periodically updates this model, generally at the request of the industry, to evaluate whether recent changes in operating costs could potentially justify a fare increase. DIER also monitors changes in the Consumer Price Index to inform this work.

Once an update of the taxi cost model is completed, DIER circulates a proposal for a fare increase (or for no increase) to the industry for comment. This proposal normally provides a comparison between the change in the cost model and the change in the CPI since the last fare increase. Once industry comments have been received, DIER reviews its proposal and makes a recommendation to the Minister for Sustainable Transport in respect of a fare increase (or no increase). If the Minister approves a recommendation for an increase, this is given effect through amendments to the Taxi Industry Regulations.

Scope of Inquiry

As per section 44 of the TER Act, the Regulator is to inquire into and make recommendations on the most appropriate methodology for:

1. Setting maximum taxi fares in the Tasmanian taxi industry; and
2. Indexing taxi fares to ensure that, over time, fares reflect the actual cost increases facing the Tasmanian taxi industry.

In undertaking the inquiry, the Regulator is to consult with key stakeholders, industry and other persons it considers appropriate.

It is recognised that this consultation process will identify a number of issues that are already seen to be directly related to the setting of fares, in addition to a range of other issues which may also be advanced as having application to the setting and indexation of fares.

The Regulator, in undertaking the inquiry, is therefore to consider the following fare-related issues:

- methods for fare setting;
- the indexation of fares; and
- the relative weighting of fare related components,

together with any other matters relating to the setting and indexation of fares which may be raised during the course of the Inquiry.

The Regulator's Final Report should also recommend:

- the period over which fares are to be indexed (the indexation period); and
- the basis on which, and the process whereby, the methodology may be reviewed before the end of the indexation period eg. where there has been a material and unforeseen change in one or more of the components relevant to determining taxi fares (including defining the threshold for determining what is a material change).

Other than as noted above, in making its recommendations the Regulator is not required to consider the impact of its recommendations on stakeholders, as these are matters for the Transport Commission and the Government ie the Regulator's role is limited to providing advice on the most appropriate method of determining, and indexing, taxi fares.

Inquiry methodology

In accordance with section 45 of the Economic Regulator Act, the Regulator may conduct the Inquiry in such manner as it considers appropriate.

Other reviews

DIER is currently two conducting other reviews relating to taxi industry regulation, these being (i) WAT fares and subsidies; and (ii) the arrangements for the release of new taxi licences.

The WAT fare review is being undertaken in response to concerns that the higher fares charged to wheelchair-reliant people travelling in WATs are discriminatory, regardless of the mitigating effect of the higher fare subsidy paid to these passengers through the Government's Transport Access Scheme (TAS). DIER has consulted with people who use WATs, disability advocacy groups and WAT operators and drivers and is currently preparing a draft report and recommendations. While the quantum of WAT fares has been considered in this review, the main focus has been on the TAS subsidies provided to passengers.

The review of taxi licence release arrangements will enter a preliminary consultation phase in the near future. It will fulfil a commitment made by DIER at the time of the commencement of the Act in 2008 to review the new licensing arrangements after a suitable period of time. The taxi industry has expressed concern that the availability of new licences has had a significant effect on the earnings of existing operators and drivers. As a result, many industry participants would like to see the Government/Transport Commission stop releasing new taxi licences.

The outcomes from these two reviews are not expected to impact directly on the taxi fare inquiry.

Date of Completion

The Tasmanian Economic Regulator is to provide a Final Report to the Transport Commission, the Minister for Sustainable Transport and the Minister for Finance by 14 December 2012 (subsequently amended to 31 May 2013).

Liability for the Costs of this Inquiry

In accordance with section 44(4) of the Economic Regulator Act, the Transport Commission is liable to pay the costs of this inquiry.

9 APPENDIX B: TREATMENT OF PLATE LEASE COSTS IN VICTORIA AND NSW

This appendix outlines the current proposals being discussed in both NSW and Victoria aimed at reducing the value of lease plates and their impact on fares.

9.1 Treatment in NSW

IPART is recently undertook a review of annual licences for Sydney on behalf of the NSW Department of Transport.

In its issues paper, IPART considered what might be classed as an unreasonable impact on existing licence holders. IPART noted that “We intend to compare licence owners’ annual returns on licences with returns on other classes of financial assets (such as government bonds, property and shares) to see whether that may give us some guidance on ‘normal’ returns, and thus on ‘reasonable’ impacts.”[45] In its issues paper IPART noted that:

- annual yields to licence holders from leasing a licence have been fairly stable at around 7.5 to 8 per cent per annum for the last ten years (the CIE estimate that the current return is approximately 7.8 per cent in Tasmania based on information collected from industry stakeholders); and
- total annual returns from leasing (lease plate revenue and capital growth) a licence have been around 12 to 14 per cent per annum and have been higher and more stable than returns offered by Australian shares.

In its draft report, IPART recommended increasing licence releases such that “income from perpetual licences could fall by 10 per cent.”[46] This was also set “in the context of a possible reduction in licence lease costs of around 25 per cent over the next 5 years”.[47] IPART also notes that “We think that an initial reduction in licence lease costs of 10 per cent provides an appropriate balance between improved affordability for operators and reduced income for licence owners”.[48] In its final report, IPART changed the mix of its recommended licence releases, however the overall impact on licence lease costs was expected to be the same. [49]

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45 IPART (2012) “Annual Taxi Licence Release for Sydney 2013/14 – Issues Paper”, p.32.

46 IPART (2012) “Annual Taxi Licence Release for Sydney 2013/14 – Draft Report”,p.44.

47 Ibid,p.44.

48 Ibid, p.4.

49 See IPART (2013) “Annual Taxi Licence Release for Sydney 2013/14 – Final Report”. Section 5.

In the short term this would not impact on fares directly, rather it is aimed to address waiting times in NSW and to induce more taxi trips from “latent demand”. Latent demand may be defined as demand for taxi trips that is not met due to higher than optimal waiting times and higher fares.[50]

In terms of fares IPART noted that it would look more closely at fare issues when it conducts its 2013 fare review. Specifically, “Last year we set the licence lease cost inflator to zero, but we would like to reconsider this and other issues in our fare review, to ensure that the objective of downward pressure on fares is met”. [51]

It is apparent that the NSW Government has not endorsed the recommendations of IPART’s licence review. Most notably, whilst IPART recommended the release of an additional 225 unrestricted licences in 2013-14 the NSW Government plans to release only 65.[52] This is slightly less than the number recommended by IPART to replace licences to be handed back or not renewed.[53] However, the NSW Government does plan to release an additional 280 peak available licences, which is 50 more than recommended by IPART which would appear to partly offset the reduction in unrestricted licences. That said, it is likely that the net impact would not have the same impact on licences values as IPART had intended.

Subsequent to this, IPART have recently released its draft report for its “2013 Review of taxi fares in NSW”. IPART has recommended that taxi fares be reduced by one per cent from July 2013. Rather than use its Taxi Cost Index and deflate lease plates by a specified amount, IPART has used a broader market model of the Taxi Industry in Sydney to determine its recommendation and analyse the impact on stakeholders. This new taxi model was developed for IPART’s licence release review, which IPART has used to consider the impact from the increase in the number of licences released and its fare recommendation. IPART considered that its Taxi Cost Index method was not achieving it aims and considered that the interaction of licence releases and fares need to be taken into account.[54] IPART consider that the one per cent reduction in fares (along with recommended changes to fare structure) will lead to a reduction in licence lease costs of approximately six per cent.[55]

9.2 Treatment in Victoria

In Victoria taxi fares were last reviewed in 2008 by the Essential Service Commission (ESC). In the 2008 review lease plates (known as assignment fees in Victoria) were included in the taxi cost model based on their value between 2000

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50 IPART (2012) “Annual Taxi Licence Release for Sydney 2013/14 – Issues Paper”, p.2.

51 IPART (2012) “Annual Taxi Licence Release for Sydney 2013/14 – Draft Report”, p.46.

52 See http://www.transport.nsw.gov.au/taxi-licence-release

53 IPART (2012) “Annual Taxi Licence Release for Sydney 2013/14 – Final Report”, p.1.

54 IPART (2013) “2013 Review of Taxi Fares in NSW – Draft Report”, p.2.

55 Ibid p.3.

and 2004.[56] This was in the context of determining fare adequacy, hence a lower than market price was used. The weight used in the model was subsequently recommended to inflate by CPI to retain its value in nominal terms. The Commission noted that "a base level assignment fee is included and indexed by CPI to ensure that the other cost items are not overrepresented"[57].

The recent Victorian Taxi Inquiry gave particular attention to the value of lease plates in Victoria and considered the impact of its recommendations on lease plate owners and consumers. The inquiry considered the view of stakeholders particularly those that had purchased lease plates as an investment or viewed it as similar to their superannuation. The inquiry outlined its views that taxi licences are not an investment like a house because there is no physical aspect to them (unlike the land the house is built on). The value of taxi licences, similar to houses, is derived from their scarcity. However taxi licences are scarce due to limited government releases of those licences.[58]

The Inquiry recommended releasing additional licences and reducing the reserve price of licence releases such that annual income from licence plates would fall to around $20 000 per year in Melbourne. This is a reduction of over 30 per cent which is higher than that recommended by IPART in NSW, at least in the short term.

The Inquiry also noted that the "most substantial financial impact would be felt by licence owners who acquired their licences after 2006"... and suggested that "the Victorian Government consider providing tightly targeted assistance to licence holders who suffer significant financial difficulties as a consequence of the reforms".[59]

Finally, the Inquiry recommended that "A review of the taxi fare setting methodology should be commenced as soon as possible. The terms of reference should have regard to the views expressed by the Taxi Industry Inquiry on fare setting methodology, should take into account the differences in industry structure between the taxi industry and other utility industries regulated by the ESC, and should consider fare setting models that account for demand factors in a dynamic way."[60]

The inquiry also responded to submissions suggesting that lease plate costs (assignment values) should be removed from the fare setting model to prevent consumers from underwriting licence values and eliminate the circularity that seems inherent in including payments to licence holders as a cost. The inquiry noted that fares are set by the regulator to recover efficient costs and thus removal would lead

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[56] See ESC (2008) "Final Report Taxi Fare Review 2007-08", p.8.

[57] Ibid p.10.

[58] See Section 3.2.2 of Taxi Service Commission (Victoria) (2012) "Customer First: Safety, Service, Choice – Taxi Industry Inquiry Final Summary Report", December 2012, for more information.

[59] Taxi Service Commission (Victoria) (2012) "Customer First: Safety, Service, Choice – Taxi Industry Inquiry Final Summary Report", December 2012, p24.

[60] Ibid p.35.

to a reduction in the fare level that would reduce licence value to zero. "The inquiry suggests that its approach of fixing assignment values is likely to have a much smoother and more predictable impact for licence holders and operators and, in the longer term, will reduce the significance of assignment fees and licence values in fares."[61] Hence, the Victorian approach may suggest assigning a zero per cent inflator to the licence value cost weight in the model, by fixing the weight (assignment value).

[61] Ibid p.185.