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REVIEW OF TAXI FARES 2007/08

INTERIM REPORT

MARCH 2008

An appropriate citation for this paper is:

Essential Services Commission 2008, *Taxi Fare Review 2007/08*: *Interim Report*, February

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EXECUTIVE SUMMARY

Background and scope of the Interim Report

On 14 January 2008 the Acting Minister for Public Transport, Mr Tim Pallas, wrote to the Commission providing amended terms of reference for the 2007/08 Taxi Fare Review. This required the Commission to provide an interim report to the Minister by 31 January 2008, or as soon as possible thereafter, on the impact of further and sustained increases in liquid petroleum gas (**LPG**) prices on taxi operators.

This Interim Report addresses this requirement. It examines whether an interim fare rise would be appropriate at the present time, and if so the magnitude of the fare rise. It also considers other sources of cost pressure in the taxi industry. Specifically, it considers the following:

- the impact of further and sustained upward pressure on LPG costs on taxi operators
- whether an immediate interim fare increase is warranted to offset rising LPG costs
- which (if any) fare components should be varied in light of these costs, and the magnitude of such variations
- the impact on the taxi industry, including licence holders, assignment holders, drivers and employees of an interim fare increase to offset these costs.

I. The impact of cost pressures from LPG prices & other sources

Before considering the impact of cost pressures it is worth outlining the different segments of the taxi industry, as the cost pressures do not necessarily have the same impact across the industry as a whole.

The participants in the taxi industry include taxi cab licence holders, fleet operators, taxi drivers, and depots/networks. Over 60% of licence holders do not operate cabs, preferring to assign (lease) them to a taxi operator who purchases, maintains and operates the taxi and delivers the service. Many operators in turn engage bailee drivers to drive some shifts, and operators often drive some shifts themselves. Bailee drivers are typically engaged under a revenue sharing arrangement.

Whilst each type of stakeholder is potentially affected by cost pressures on the taxi industry, it is operators in the first instance who are likely to bear the direct impact of pressures such as rising LPG prices and licence assignment fees.

LPG prices were around 40% higher in January 2008 compared to January 2007 and around 20% higher than the previous peak in February 2006. While LPG prices have spiked in recent months, there are typically peaks in most summer periods, associated with winter heating demand in the northern hemisphere.

LPG prices may be expected to ease in the coming months as the northern hemisphere enters the spring season. Overall, lower recent Saudi Aramco contract prices for Propane and Butane (the major components of LPG) and recent futures contract prices on the New York Mercantile Exchange (**Nymex**) indicate the market expects a combined decrease in LPG prices of 12-13% from their January peak over the coming months.

However, while prices are expected to ease to around 60 cent per litre (cpl) over the period February to June 2008, based on the Nymex futures, they will still be approximately 18% higher than the average for calendar 2007.

Between the June quarter 2005 and the December quarter 2007, LPG prices are estimated to have added an additional 3.8% to taxi operator costs.

In addition to the 3.8% impact on costs associated with LPG prices, there have been increases in licence assignment fees that have also impacted on taxi operator costs. Comparing current licence assignment fees to the PwC estimate in 2004 indicates an average annual increase of around 8% over the last three years, with a total increase of 25%. The estimated increase in monthly licence rental costs is approximately $475, representing an increase in operator costs of around 4.5%.

It should be noted, that the Commission views assignment fees as a matter relating to the distribution of the total taxi industry income between industry participants. As such, it should not represent a basis for increasing taxi fares to the public.

Cost pressures and current fare levels

A broad based survey of taxi operators and drivers has been carried out by PricewaterhouseCoopers (**PwC**), with 431 responses. PwC's analysis of the survey returns (Appendix C) indicates that taxi operator margins in 2007 averaged approximately 8% over costs.

In recent months taxi operator margins have been squeezed, primarily due to the spike in LPG prices, and in the previous three years, increases in assignment fees.

Leaving aside changes in assignment fees, and taking into account an easing in the price of LPG, margins for taxi operators will have reduced from the 8-10% assumed in recommending fare increases in 2005 to around 8% by June 2008.

The results of the PwC survey show that operator margins in 2007 remain within a range that is not uncommon in trading businesses with low degrees of capital intensity (3-8%).

However, there are two important observations to make in relation to the survey results:

- While it could be argued that these projected margins could be sustained until fares are determined later this year, the cost increases due to LPG prices were not anticipated in 2005 when the prevailing price path was put in place and as a consequence the margins have reduced markedly.

- A degree of care needs to be taken in relying on survey results as an accurate predictor of actual margins because of the sample size[1].

With this in mind, the Commission estimates that the combined impact of increased LPG prices and costs of complying with recent changes to regulations for industry accreditation is in the order of 4% on total operator costs.

A more detailed analysis of whether a “catch-up” price adjustment is warranted in September, as well as other options to alleviate cost pressures associated with increasing licence assignment fees are matters that will be given consideration by the Commission in the Draft and Final reports of this Review.

Country Taxi Fare levels

The PwC survey found that taxi operator margins in the major regional centres (Geelong, Ballarat and Bendigo) are higher than in the metropolitan area, but operator margins in the other country areas (i.e. the ‘Country’ fare zone) are only 1% over costs. Taxi operating costs were similar to metro levels, but fare revenues were around 7% lower.

The Commission is of the view that this result needs to be considered in light of the observation that in the country, taxis are typically operated by the licence holder – not by a third party to which the licence is assigned. In the country areas licence assignment fees were found in the survey to be surprisingly high, representing 17% of costs. The combined return to the licence holder/operator was approximately 18% of revenue in 2007.

The 2006 Country Taxi Review expressed concern about the financial viability of operators in rural and regional Victoria in towns where small population sizes (and thus limited demand) have an impact on operating revenue. Were those towns to lose their taxi operators, they may not be replaced. As such, the risk that such communities might not have any form of public transport must be a concern. In part an appropriate response may be to provide greater pricing flexibility and access to licences for taxi operations in these areas. Relevant options will be considered in the Draft and Final reports of this Review.

II. Options for the Government in responding to the impact of LPG costs on taxi operators

Recent LPG price movements not only have implications for whether the existing level of taxi fares adequately provides for the recovery of costs, it also has relevance for some other questions to be addressed in the Review, such as the requirement for the Commission to identify a preferred *price adjustment formula* which provides for automated fare adjustments over a three to five year period.

Such a formula will need to adequately deal with the volatility of LPG prices over a 3-5 year period. The possible approaches to the future fare adjustment formula need to be taken into account when considering the options for responding to the

[1] PwC notes (p.7) that at a 95% confidence interval the costs and revenue results could vary by up to 6.8%.

impact of LPG costs on taxi operators. Some of the options for responding to LPG costs are outlined below. In relation to fare adjustment formulas, some preliminary views are expressed, and a fuller consideration will be given in the Draft and Final reports of this Review.

(a) LPG fuel price levy (as suggested by the VTA)

The Victorian Taxi Association (**VTA**) has suggested the adoption of a fuel price levy, similar to those used in the airline industry, with quarterly adjustments made by the government in line with LPG price increases. If at any time in the future the price of LPG was to fall the levy would be removed.

Such an LPG price-related levy would have the benefit of providing an ongoing means of alleviating future fuel price movements. The proposed quarterly price adjustments would better align fares with movements in costs than less frequent adjustments.

At this stage, the Commission believes that this may not be the best of the available options for the longer term, because:

- it would not be consistent with having a predetermined formula and process that provides certainty for the taxi industry and for users, as previously recommended by the Commission
- it is not used in any other Australian taxi jurisdiction
- the significant degree of month-to-month volatility in LPG prices is likely to lead to considerable administrative costs and taxi fare volatility, and potentially add to taxi operator costs
- it may not be viewed favourably by customers, considering there are already a range of add-ons to taxi fares (e.g. credit card charges, airport fees, tolls etc).

However, it may be an appropriate short term measure to alleviate immediate financial pressures on taxi operators associated with increased LPG prices. The question of an interim price increase is addressed below.

(b) Interim fare increase

The terms of reference direct the Commission to assess the impact of sustained increases in LPG prices. The Commission has estimated that LPG costs have added 3.8% to taxi operator costs between the June quarter 2005 and the December quarter 2007. As the December quarter 2007 average LPG price is considered to be representative of LPG prices in coming months, this is also an estimate of the sustained impact of LPG prices on taxi operator costs. Taking into account the costs of industry accreditation compliance indicates approximately an additional 4% in total to the costs of an ‘average’ taxi operator.

The Commission has been asked to advise whether an interim fare increase is warranted. These cost increases were not anticipated in 2005, and as such, operator margins are somewhat lower than expected when the prevailing price path was put in place. This is a matter that the Commission would consider in making its final recommendations in June 2008. However, an interim fare adjustment would provide an immediate response to the impact of LPG prices on taxi operator margins.

Taking the impact of LPG prices and the accreditation compliance costs together, the Commission's estimate of the required catch up fare increase at the present time is approximately 4%.

In its reviews the Commission has emphasised that the distribution of income within the taxi industry should be treated as a separate matter to setting taxi fare levels. Therefore, distributional considerations should not affect the quantum of any fare increase.

Nevertheless, a key concern of the Commission is the likely capture of any fare increase by licence holders, and possibly depots/networks, whereby fees payable by operators are increased commensurately. This would simply result in taxi users facing higher charges (and possibly reducing their levels of patronage), higher returns to licence holders and taxi operators getting little of the intended benefit. Given the turnover rates of existing assignment contracts (which have an average term of approximately one and a half years) this form of flow-through may be relatively moderate over the few months prior to the Commission completing its Final Report to the Review, which will address issues relevant to the distribution of income in the taxi industry.

Another concern is the extent to which any revenue increase flowing from an interim fare increase is likely to flow to taxi operators, who incur LPG costs. Under existing bailment arrangements 50% of any revenue gain would flow to operators and 50% to drivers. However, it is also observed in chapter 4 that drivers are in a relatively weak bargaining position, and that bailment terms may alter. Given this, the Commission has concluded in chapter 4 that there is a risk that drivers may not achieve all of this gain if bailment arrangements change. Taxi operators therefore may be the primary beneficiaries of a fare increase in the short term, but given the tendency for rents to flow through to assignment fees under current market and regulatory arrangements, taxi operators cannot be expected to retain those gains over time.

Given this assessment there does not appear to be a strong benefit, in the short-term, to options designed to 'quarantine' any revenue gains from a fare rise to taxi operators. Ensuring that any revenue increase flows only to taxi operators would either require direct controls over bailment contracts or licence assignment fees – in each case a significant intervention – or a form of levy that is not captured by the provisions in existing bailment or assignment agreements which may otherwise pass through part of any increase in revenue to drivers or licence holders.

As discussed in section 6.3 increased regulatory controls are only one approach to addressing the wider issues in relation to income distribution in the industry which the Commission will examine as part of the Review. A comprehensive review of the options for improving taxi operator and driver remuneration will be covered in the Draft and Final Reports of this Review.

On the question of whether a levy can be structured to 'quarantine' gains to taxi operators, one approach that has been flagged by stakeholders is the option of an 'off meter' levy. This approach would have the benefit of removing the need for adjustment of taxi meters (thereby avoiding the cost of doing so), but has a number of drawbacks in terms of lack of transparency, increased administrative costs of manual settlement transactions, and greater costs of handling of customer complaints by taxi drivers and relevant bodies. Instead, the Commission recommends that the cost of adjusting a taxi meter (estimated to be $140 by industry participants), be factored into any interim fare increase, and that any fare increase be 'on meter'. The Commission estimates the recovery, over a six month period, of the cost of adjusting a taxi meter would represent 0.2% of revenue based on PwC's estimate of the annual revenue for a median taxi cab. Therefore, the required fare increase would be 4.2%.

In relation to the potential demand response to an interim price increase, the Commission will give consideration in the Draft and Final reports to the benefits of a maximum fare regime in the pre-booked market, which may enable taxi operators to mitigate risks of a potential demand response by discounting fares, if this is found to be necessary or advantageous.

Other options to alleviate cost pressures or improve the ability to increase revenue will also be considered in the Draft and Final reports. This includes the impacts that increasing assignment fees can have on the ability of the industry to compete and provide high service standards.

Summary – required 'catch-up' fare increase

Although the broader question of fare adjustment is a matter that the Commission will consider in making its final recommendations in June 2008, an interim fare adjustment would provide an immediate response to the impact of LPG prices on taxi operator margins.

Taking the impact of LPG prices and the accreditation compliance costs, together with the costs of meter adjustment, the Commission's estimate of the required 'catch up' fare increase at the present time is approximately 4.2%. If an interim fare increase is to be made, this is the Commission's recommendation as to the amount of the fare adjustment.

(c) Composite index approach

The examination of recent cost pressures, and the assessment of whether an interim increase is needed, has highlighted the importance of implementing a mechanism to adjust fares with reference to movements in input costs over time.

In the Issues Paper the Commission canvassed three options for fare adjustment over the next 3 to 5 years:

- an industry-specific cost index used to determine future fare increases in line with the movement in the principle costs of a taxi business (e.g. fuel consumption and prices, parts and maintenance costs, insurance, etc.)
- a composite index of input prices from published sources
- the current CPI-X method, with the X factor accounting for taxi industry productivity gains.

The Commission sees merit in the use of a specifically constructed composite index of input prices for fare adjustments over the next 3 to 5 years. This would use a small number of published price indices relevant to Victorian taxi industry costs, including LPG price indices. Each index would be appropriately weighted to reflect relative importance of the inputs in total costs.

The Commission's preliminary view is that a productivity adjustment would remain appropriate within this model, to ensure that the fare escalation formula remains cost-reflective over the pricing period. Such a composite index will also require periodic re-weighting every 3-5 years to remain a reasonably accurate reflection of the taxi industry cost mix.

The approach would be relatively simple to administer as it relies on price indices published by the Australian Bureau of Statistics and published LPG prices. It would also provide certainty for the taxi industry and for users, as it is a predetermined formula using publicly available information. It would also provide strong incentives for efficiency improvement, as annual fare adjustments during the 3-5 year pricing period would not be influenced by taxi industry cost outcomes (which would weaken the incentives to achieve cost efficiencies).

The timing of fare adjustments is a matter the Commission must make recommendations on in its Draft and Final reports.

III. Fare component Variations

Stakeholders have raised a range of issues in relation to fare structures. The Commission will give consideration to the fare structure in the Draft and Final reports of this Review. Given this, and the Commission's preference for the implications of cost pressures in the taxi industry to be given further consideration in the Review, the issue of fare component variations has not been addressed in this Interim Report. As some of the "fixed" elements of the fare structure may recover some of the on-road costs of cabs, it should not be assumed that only the per-kilometre charge would be relevant to an interim price adjustment.

The Commission's preference is for the alternative options to be given further consideration in the Review. If there is an interim price increase, then the Commission's preference is that, prior to its findings on fare structure in the Draft and Final reports of this Review, any fare increase should be applied proportionately to all charges on the metered fare (i.e. a 4.2% increase to each fare component). However, should this recommendation not be accepted, Table 6.1 shows several examples of alternative ways for effecting a 4.2% increase, including: a 6.2% increase in the distance charge alone; a 24.7% (i.e. 77 cents) increase in the flag-fall alone; a 20.4% increase in both the flag-fall and the booking fee; or a 50% increase in the booking fee and a 3.6% increase in the distance charge, among other options.

Table 6.1 (reproduced) **Fare adjustment options**

			Revenue per fare component per trip					
	Current fare components	*Factor[a]*	*Current fare*	*Increase all charges by 4.2%'*	*Increase in distance charge only by 6.2%*	*Increase in flagfall only by 24.7%*	*Proportionate increase in flagfall & booking fee by 20.4%*	*Increase in booking fee by 50% and distance charge by 3.6%*
Flagfall	3.10		3.10	3.23	3.10	3.86	3.73	3.10
Distance charge	1.47	8.4 km	12.35	12.87	13.11	12.35	12.35	12.79
Booking fee	1.30	50% of trips	0.65	0.68	0.65	0.65	0.78	0.98
Waiting time charge	31.5	3.0 min	1.58	1.64	1.58	1.58	1.58	1.58
Late Night Surcharge	20%	15% of trips	0.53	0.55	0.53	0.53	0.53	0.53
Total			18.20	18.97	18.97	18.97	18.97	18.97

a Sources: PwC 2007 survey, VTA

IV. Implications of fare increases for users and taxi industry participants

The implications of fare increases for users also needs to be taken into account, particularly those dependent on taxis, such as elderly or disabled users. Submissions indicate that the interest of these users is in having regular and predictable fare increases, and in the financial sustainability of taxi services.

The distribution of fare increases between industry participants will be strongly influenced by the existing market power imbalance in the industry.

Under current bailment arrangements, driver incomes (and the incomes of operators in their capacity as drivers) can be expected to increase proportionately to industry revenue, as drivers typically retain around 50% of revenue. However, given drivers tend to be in a relatively weaker bargaining position, there is a risk that they may not achieve all of this gain if bailment arrangements change.

Recent increases in assignment fees appear to be at odds with expectations of an efficiently functioning licence assignment market. Licence assignment fees should fall when operator costs rise. Although existing assignment contracts may result in lags, there may also be some downward resistance to licence rental costs. If so, this may be associated with the imbalance of market power in the industry. Increased depot/network consolidation has been accompanied by increases in network fees averaging over 5% per annum over the last three years. Licence holders appear to hold sufficient market power to capture most of the available economic rents, given the constraints to the availability of new licences.

In the current highly concentrated market, there is reason for concern that the main impact of a price rise on industry participants will be to enhance the returns for the segments of the industry with market power, namely the licence holders and the depot/networks. Taxi operators cannot be expected to gain significantly from a price rise.

Summary of Conclusions

The Commission's analysis suggests that there are a number of factors impacting taxi operator returns in addition to LPG prices, not least of which is the cost of renting a taxi licence. Licence values and assignment costs have increased rapidly in recent years, and in light of these trends, further attention needs to be given to options to address this source of cost pressure. Some options have been suggested by submitters, such as changing the current licence marketing arrangements, and these and other options deserve examination in the Draft and Final Reports of this Review. The sources of increased licence assignment costs and the options to reduce them need to be given careful consideration.

More broadly, the regulatory framework appears to impose some restrictions which may impede the ability of taxi operators to achieve revenue growth, or may be detrimental to driver incomes. A number of options are to be examined in the Draft and Final Reports for increasing the flexibility of taxi operators, and to facilitate efficiency.

The Commission has reached the following conclusions in preparing this Interim Report regarding recent increases in LPG prices. It should be stressed that in reaching these conclusions the Commission is currently undertaking a review which is to examine a broader range of considerations, including driver remuneration, affordability and availability of taxi services. There have been a number of submissions made in relation to these matters, which will be considered through a consultative process in the coming months. Hence, the following conclusions should be regarded as recommendations to deal with a specific issue of concern at this point in time, and should not be seen as pre-determining the outcomes of the overall review.

- The impact of recent increases in LPG prices and accreditation costs is approximately 4% of the total revenue required to operate a taxi and earn a margin (net of assignment fees) commensurate with the level adopted in 2005.
- The increase in the price of LPG is borne entirely by taxi operators, who have also faced increasing assignment fees payable to licence holders.
- Increased input costs since the last review of taxi fares are expected to result in increased fares in 2008.
- After setting fares for 2008, the subsequent adjustment of fares over the next 3-5 years should occur through a pre-determined automated price formula linked more closely to taxi input costs.
- The movement in assignment costs is a matter that relates to the distribution of income between licence holders and taxi operators, and should not warrant changes to the fares paid by taxi users.
- The use of the CPI-X formula has resulted in lower margins for operators than expected, since taxi input costs have grown at a faster rate than the CPI.
- An interim fare increase would alleviate the impacts of increased costs on taxi operators, provided that assignment fees are not increased proportionately.
- A separate levy is not preferred as a long term option, although it could be considered as an interim measure if it provides a means to ensure that this additional revenue is retained by taxi operators
- The merits of a ‘catch up’ increase to offset the unforeseen increases in costs since 2005 will be considered by the Commission in preparing its final report in June 2008, and this will take into account any decision made in relation to an interim increase.

1 INTRODUCTION

The Victorian taxi industry is subject to regulation under the *Transport Act 1983*. Under this framework each taxi operator must be licensed and the taxi fares are set by the Minister for Public Transport[2] under s.144A(1) of the Act.

The taxi fares set by the Minister must be charged by the cab[3], although an exception is made for permanent and contracted services where operators and drivers can negotiate fares below the metered rate.

Under s.144A(2) the Minister for Public Transport, prior to changing the schedule of taxi-cab fares, must obtain advisory reports from the Commission and the Director of Public Transport.

1.1 Terms of reference

This report has been prepared in response to the terms of reference for the Taxi Fare Review. The Review was initially notified to the Commission on 19 September 2007 by the Minister for Public Transport, and subsequently amended by notice from the Acting Minister for Public Transport to the Commission on 14 January 2008. The full terms of reference are presented in Attachment A.

In summary, the Acting Minister for Public Transport has given notice that in accordance with the provisions of section 186 of the *Transport Act 1983*, the Commission is required to conduct an investigation into Victoria's taxi-cab fares and report on:

i. the impact of further and sustained upward pressure on liquid petroleum gas (LPG) costs on taxi operators;

ii. an appropriate price setting model to provide for automated fare adjustments for the next 3–5 years, including the timing of such adjustments;

iii. the appropriateness of the taxi fare structure within the current market for taxi-cab services in Victoria;

iv. whether a surcharge on taxi fares on New Year's Eve should form a permanent part of the taxi fare structure for non-metropolitan taxi-cabs and, if so, the amount of such surcharge;

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[2] This is a condition of the taxi cab license as provided for under s.144(2)(d) of the Act.

[3] This mandatory fare approach is not typical in Australia. In most other jurisdictions where taxi fares are regulated, these are maximum fares, which the taxi operator can discount from. This is relevant to the detail comparison of taxi fares in chapter 5.

v. whether a surcharge on taxi fares should form a permanent part of the taxi fare structure where the hirer pre-books and is supplied a premium service taxi and, if so, the amount of such surcharge;

vi. the distribution of taxi fare revenue and measures that may be considered by Government to improve taxi driver remuneration; and

vii. information reporting by the taxi industry and performance measurement.

In undertaking the review, the Commission is required to take into consideration several matters including:

- the cost pressures on the industry regarding the increase in the price of LPG
- the findings of its Taxi Fare Review 2005 and the country taxi review undertaken by the Department of Infrastructure (**DOI**) in 2005/06
- the impact on Victorian business and the community, the taxi industry and to issues such as the availability and affordability of services to customers, and
- the impact on taxi industry participants including licence holders, taxi operators, drivers and employees.

The Commission must also have regard to its statutory objectives in s.8 of the *Essential Services Commission Act 2001* (**ESC Act**), and must provide its final report to the Minister by 30 June 2007. In addition, an interim report in respect of the impact of LPG prices must be provided to the Minister by 31 January or as soon as possible thereafter.

The specific matters that were the subject of the amendment to the terms of reference were the requirements:

(1) to report on “the impact of further and sustained upward pressure on liquid petroleum gas (LPG) costs on taxi operators”, and to have regard to “the cost pressures on the industry regarding the increase in the price of LPG”

(2) provide an interim report in respect of the impact of LPG prices by 31 January or as soon as possible thereafter.

The Minister’s letter states that the interim report should provide advice to the Minister on whether an immediate interim fare increase is warranted to offset rising LPG costs, and if so, which fare components should be varied and the magnitude of the variations.

1.2 Purpose of the Report

This report satisfies the requirement in the terms of reference to provide advice on the impact of LPG prices, and whether an immediate interim fare increase is warranted, and if so the magnitude of the increase, and other matters relevant to the cost pressures on the taxi industry.

Specifically, it considers the following:

- the impact of further and sustained upward pressure on LPG costs on taxi operators

- whether an immediate interim fare increase is warranted to offset rising LPG costs
- which (if any) fare components should be varied in light of these costs, and the magnitude of such variations
- the impact on the taxi industry, including licence holders, assignment holders, drivers and employees of an interim fare increase to offset these costs.

1.3 Scope of the Report

The question of the adequacy of the current fare levels which the Commission must address under item (i) of the terms of reference, and report on in this Interim Report, is related to the approach that the Commission proposes to take in relation to considering the future path of fares – under item (ii) of the terms of reference – as follows.

The Commission's overall approach to these two elements of the terms of reference will be to:

- firstly, examine whether the existing level of taxi fares adequately provides for the recovery of costs, and
- secondly, to identify a preferred price adjustment formula which provides for automated fare adjustments over a three to five year period.

This report addresses the first of these issues with respect to the question of an interim price rise, and presents the Commission's recommendations. In relation to the second issue, this report reiterates the options being considered by the Commission, and outlines its preliminary preferred approach.

Other elements of the terms of reference are not substantively addressed in this report. These include:

- the structure of taxi fares and the surcharges, including for premium services and New Year's Eve services (items (iii), (iv) and (v))
- options to improve the remuneration of drivers (item (vi))
- information reporting in the taxi industry and performance measurement (item (vii)).

Although these questions are not covered in this report, they are connected to the issue of fare levels. For example, the assessed cost impact of new accreditation arrangements on the industry will be relevant. Hence the question of the adequacy of fare levels will be given further consideration in the Draft and Final Reports having regard to a wider set of issues.

Also, the Commission is required to have regard to the impacts of its recommendations (including with respect to an interim price adjustment) on industry participants and the distribution of any additional income between taxi industry participants.

In summary, this report contains recommendations on the questions of whether there should or should not be an interim taxi fare increase, and whether there should be an LPG Levy, as suggested by the VTA. On some of the other matters the Commission may present some preliminary views to be further developed in the Draft and Final Reports.

1.4 Relevant Statutory Objectives

The terms of reference direct the Commission to have regard to the objectives of the Commission in s.8 of the ESC Act. The Commission's primary objective is to protect the long term interests of Victorian consumers with regard to the price, quality and reliability of essential services. Its facilitating objectives include:

- to facilitate efficiency in regulated industries and the incentive for efficient long-term investment;
- to facilitate the financial viability of regulated industries;
- to ensure that the misuse of monopoly or non-transitory market power is prevented;
- to facilitate effective competition and promote competitive market conduct;
- to ensure that regulatory decision making has regard to the relevant health, safety, environmental and social legislation applying to the regulated industry;
- to ensure that users and consumers (including low-income or vulnerable customers) benefit from the gains from competition and efficiency; and
- to promote consistency in regulation between States and on a national basis.

1.5 Previous Taxi Fare Review

In 2005 the Commission undertook a review of taxi fares that was submitted to the Minister for Transport in June 2005. The terms of reference of that review required the Commission to assess the existing fare structure and to recommend appropriate variations to each fare component, having regard to the impact on Victorian business and the community, the taxi industry, and regional communities.

In the *Taxi Fare Review 2005 Final Report*, the Commission made a number of recommendations to the Victorian Government. With respect to the level of taxi fares, the Commission recommended an immediate increase of 8%, as a "catch up" in the absence of fare increases between 2000 and 2004. It also recommended that in the following two years the level of fares should be adjusted by the Consumer Price Index (**CPI**) minus 1%. The 8% fare increase was subsequently given effect in September 2005. The fare increases in September 2006 and September 2007 were 3% and 1.1% respectively, in accordance with the CPI-1% formula.

In relation to future fare setting, the Commission recommended that this should be based on a predetermined formula and process that provides certainty for the taxi industry and for users. This recommendation was endorsed by the Government. This is one of the matters that the Commission must have regard to in this Review.

1.6 Process for conducting the Review

Section 187 of the *Transport Act 1983* specifies the manner in which the Commission must undertake its investigations. The Commission may conduct an investigation in any manner it deems appropriate, may receive written submissions or statements, hold public hearings and may consult with any person that it considers appropriate.

An Open Letter was published on 10 October 2007 informing the public of the review and outlining the timeframes that the Commission adopted. An Issues Paper was released on 3 December 2007.

A period of eight weeks was provided for public submissions[4]. Submissions to the Issues Paper were received from: two taxi drivers Mr David Griffiths and Mr Wally Hunt, the Department of Human Services (**DHS**), the Department of Infrastructure (**DOI**), the Victorian Council of Social Service (**VCOSS**), the Victorian Taxi Association (**VTA**), the Victorian Taxi Directorate (**VTD**), and Mr David Walsh.

The key dates for the review are in Table 1.1 below.

Table 1.1 **Timetable to conduct the Review**

Timeframe	**Task**
19 February	Public hearing in Bendigo
26 February	Public hearing in Melbourne
4 March	Public hearing in Morwell
March–April	Release of *Draft Report* (including draft recommendations) for four week consultation period
Within 4 week of release of draft report	Submissions to *Draft Report*
30 June 2008	Delivery of *Final Report* to Minister

Under section 190 of the *Transport Act 1983*, the Minister must make the Commission's Final Report public within seven sitting days of Parliament or within 30 days if Parliament is not sitting. However, the Act does not require the Minister to accept the Commission's recommendations or specify when the Minister must make a decision about the adjustment of taxi fares following receipt of the Commission's advice.

1.7 Plan of the report

The remainder of this Interim Report has the following structure:

- Chapter 2 describes a number of cost pressures recently impacting on the taxi industry, and market mechanisms that are relevant to mediating those pressures
- Chapter 3 presents the analysis and estimates of taxi operator costs and returns, as well as trends in unit costs compared to fares
- Chapter 4 discusses the possible impacts of a fare increase on users of taxis and on taxi industry participants

[4] In relation to comments made by the VTA in relation to the adequacy of the consulting period, it should be noted that the period of 8 weeks provided for submissions was considerably longer than the minimum consultation period of 3 weeks stated in the Commission's *Charter of Public Consultation and regulatory Practice*, thereby adequately allowing for the Christmas/New Year period.

- Chapter 5 examines the costs and returns of taxi operators in country Victoria, and
- Chapter 6 contains the Commission’s recommendations on the question of an interim price increase, and its preliminary views on a number of related issues.

2 RECENT COST PRESSURES

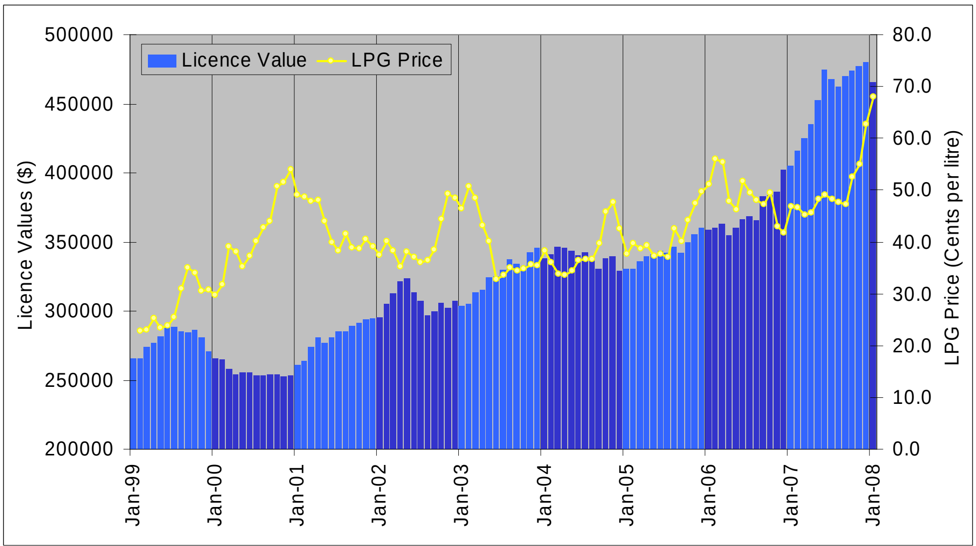
This chapter examines recent cost pressures on the taxi industry and the implications of these trends for future fare setting and taxi industry regulation.

The chapter first discusses recent trends in LPG prices and licence assignment fees in section 2.1. The future outlook for LPG prices is discussed in section 2.2. The important role of the market for assignment (renting) of taxi licenses is discussed in section 2.3. Then section 2.4 summarises the conclusions relevant to questions addressed in this report.

2.1 Impact of LPG price trends & licence values

Taxi operator costs have been impacted in recent times by LPG price movements and licence rental costs. Figure 2.1 shows monthly average LPG prices and licence values. LPG prices have spiked in recent months although there is typically a summer peak associated with winter heating demand in the northern hemisphere. Licences values have increased strongly in recent years, and are currently close to $500,000 each (and now considerably higher than in Sydney). The chart shows that licence values appear to have reached a plateau over recent months, with the latest month of data showing a small decline on a thinly traded market.

Figure 2.1 **LPG price & taxi licence value 1999-2008**



Data sources: FuelTrac, BSX Taxi Market, VTD

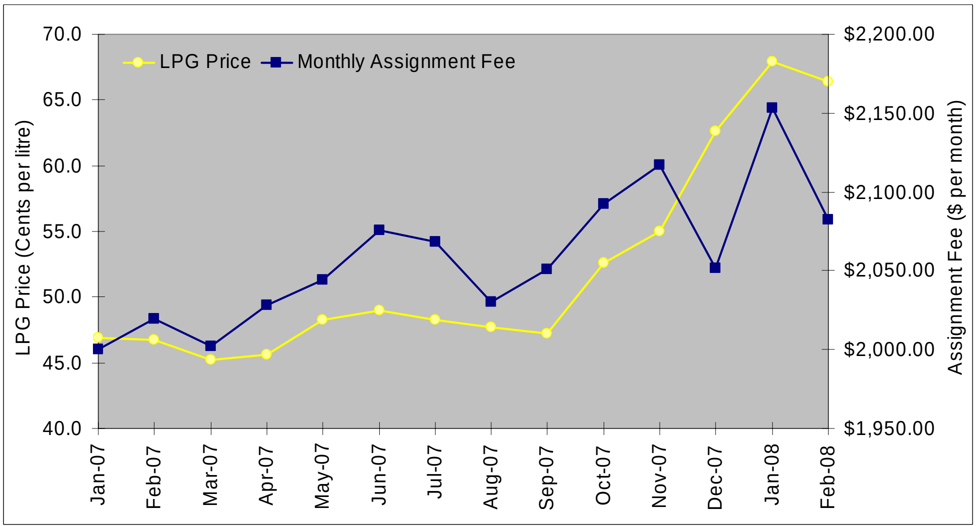
Figure 2.2 shows monthly averages of LPG prices and licence assignment costs since January 2007. This data shows licence assignment fees have increased over this 12 month period by around 8%. LPG prices are around 40% higher in January 2008 compared to January 2007 (and around 20% higher than the previous peak in February 2006).

By way of simplistic quantification of the impact of the LPG price, the rise since the last fare adjustment (22 September 2007) from 47 cents per litre (cpl) to 66 cpl (assuming an average distance travelled of 140,000km pa at an average consumption of 5 km/L) generates an increase in monthly LPG costs of approximately $440 – representing a 4% increase in taxi operator costs. Recent indicators suggest declines in wholesale LPG prices since that time which will reverse trends in LPG prices over the coming months (see section 3.2).

Comparison of current licence assignment fees (approximately $2,150 per month for new assignment contracts in January 2008) to the PricewaterhouseCoopers (**PwC**) estimate of licence assignment fees in 2004[5] (i.e. $1715) indicates there has been an average annual increase of around 8% over the last three years, with a total increase of 25%. The estimated increase in monthly licence rental costs is approximately $475, representing an increase in operator costs of around 4.5%.

In both cases these are gross cost increases, rather than unit cost increases. The implications for unit costs are more relevant to taxi fares, and these are discussed in more detail in Chapter 4.

Figure 2.2 **LPG price & licence assignment fee 2007-2008[a]**



[a] February data is incomplete.

Data sources: FuelTrac, BSX Taxi Market

[5] PwC (May 2005) 'Report to the ESC on changes on costs of operating taxis in Victoria'

Summary conclusion:

Taxi operator costs are being impacted by cost pressures from both LPG prices and licence assignment fees.

2.2 Forecasts of LPG prices

While LPG prices have increased significantly in the months since the last taxi fare increase in September 2007, the Commission must not only have regard to price increases already observed, but also what is likely to happen in the immediate future to fuel costs. In the context of this Interim Report, the Commission specifically has an interest in understanding the direction and impact of LPG prices until the end of the current financial year (i.e. the remainder of the pricing period).

As noted earlier, LPG prices typically spike during the summer months. Significant jumps around this time have been observed in at least five of the last eight years. This is not unusual in the context of energy prices in general, as this corresponds with winter in the northern hemisphere and a greater demand for heating fuel. On this basis, it would be reasonable to assume some degree of easing in LPG prices in the coming months as the northern hemisphere enters the spring season.

The benchmark for Australian LPG prices is the Saudi Aramco contract price, which are set at the start of each month. The January contract price for propane (which is the major, although not the only component of LPG) was US$870 a metric ton. The latest contract price for February is US$800. This indicates that LPG prices have peaked, and that consumers should expect a fall in retail LPG prices of approximately 8% during February.

Expectations of a price fall are supported by more detailed market intelligence. Financial news service Bloomberg reported on 25 January that wholesale LPG prices in Asia had fallen during the month, with significantly weaker demand from China for LPG imports[6]. This is reinforced by analysis from consultants Poten & Partners which announced in October a bearish outlook for China's LPG demand. It also noted that the supply of LPG is likely to increase as a result of increased production[7]. A reduction in demand and an increase in supply, all else being equal, will result in lower prices.

There are limited indicators which can be used to quantify the possible decline in LPG prices over the coming months. Of these, perhaps the best projection might come from futures contracts on the New York Mercantile Exchange for Liquefied Propane Gas – as shown in Table 2.1. These suggest that the market expects the average propane price during the period March to June will be approximately 3.5% lower than the contract price in February. Overall, the recent contract prices and

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[6] Bloomberg 2008, 'Asian LPG Declines After China's Imports Slump to 10-Year Low', 25 January. http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a_O5CIoaDXzo

[7] Poten & Partners, 2007 'Poten's New LPG Forecast', 15 October. http://www.poten.com/show_articles.asp?id=634&table=tmarket

the futures contract prices indicate that the market expects a combined decrease in LPG prices of 12-13% from their January peak over the coming months.

Table 2.1 **NYMEX Propane Futures**

As at 7 February

	Monthly Change	*Cumulative Change*
February[a]	-8.80%	-8.80%
March	-7.78%	-15.90%
April	-1.65%	-17.28%
May	5.41%	-12.81%
June	-0.18%	-12.96%

[a] Based on last closed trade on February futures contracts.

Data source: New York Mercantile Exchange

Summary conclusion:

Recent bulk contracts and futures contracts suggest that the market expects LPG prices to decrease by more than 10% in coming months.

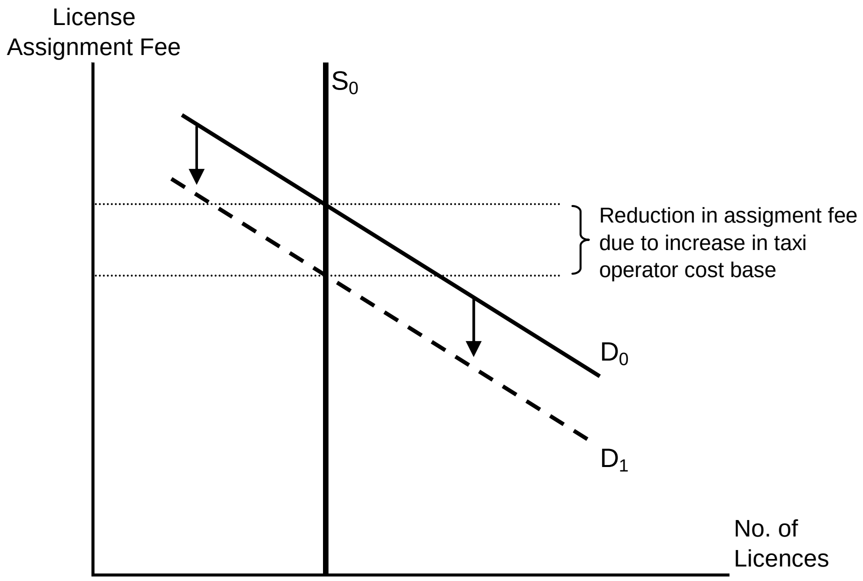
2.3 The market for renting licenses

The observed trends indicate that recent increases in licence assignment costs are a significant source of higher costs in addition to LPG prices. Assignment fees were estimated by PwC to represent 16% of total taxi operator costs in 2004 and with the recent average increases of around 8% per year noted above, they may now represent around 20% of costs for a conventional cab with a newly assigned licence (not including “green tops”). By contrast, the 2007 PwC analysis of taxi costs in metro NSW has plate assignment (lease) costs at 13% of total costs.

Most licenses are in private hands and assigned to taxi operators for a fee (more recently issued peak period licenses are rented from the government for an annual fee). The licence assignment cost to operators arises due to the limited number of taxi licenses and large number of potential taxi operators.

The market forces of supply and demand for licences suggest that if taxi operator costs rise (e.g. due to LPG price increases) then, in the market for licenses, the demand for licenses will decrease and the assignment fee should fall – as shown in Figure 2.3.

Figure 2.3 **Theoretical effect of increases in operator costs on license assignment fees – market for licence rental**



The information presented in Figure 2.2 above indicates that some downward pressure on assignment fees is beginning to emerge in February 2008, following the increases in taxi operator costs imposed by LPG prices. If sustained, such reductions in licence assignment fees will partly mitigate taxi operator cost pressures.

Preliminary conclusions:

The market for licenses should ensure that assignment fees fall when operator costs rise (e.g. due to LPG prices). There is some evidence in February assignments that licence rental costs are beginning to adjust downward in the face of increases in operator costs.

The functioning of the market for licence assignment can be expected to ensure that within the metropolitan market, there is relatively low risk that the overall level of taxi supply will be affected by cost pressures. Even though there may be some resistance to reductions in licence rental fees to absorb increases in operator costs, licence holders will always need to assign available licences. However, the same mechanism may not necessarily apply in all country areas. The scaling back of operators or exit of a taxi operator in a country town could potentially lead to a reduction in available services.

3 TAXI OPERATOR COSTS

In considering the question of the adequacy of current fare levels to provide for the recovery of costs and acceptable levels of driver incomes, the Commission has taken the following approaches:

- benchmarking taxi fares against trends in fares for public transport, and against taxi fares in other Australian capital cities.
- direct estimation of taxi operator costs based on a survey of operators and drivers
- historical comparisons of trends in taxi fares and estimated unit cost trends.

This chapter describes the results of each of these approaches.

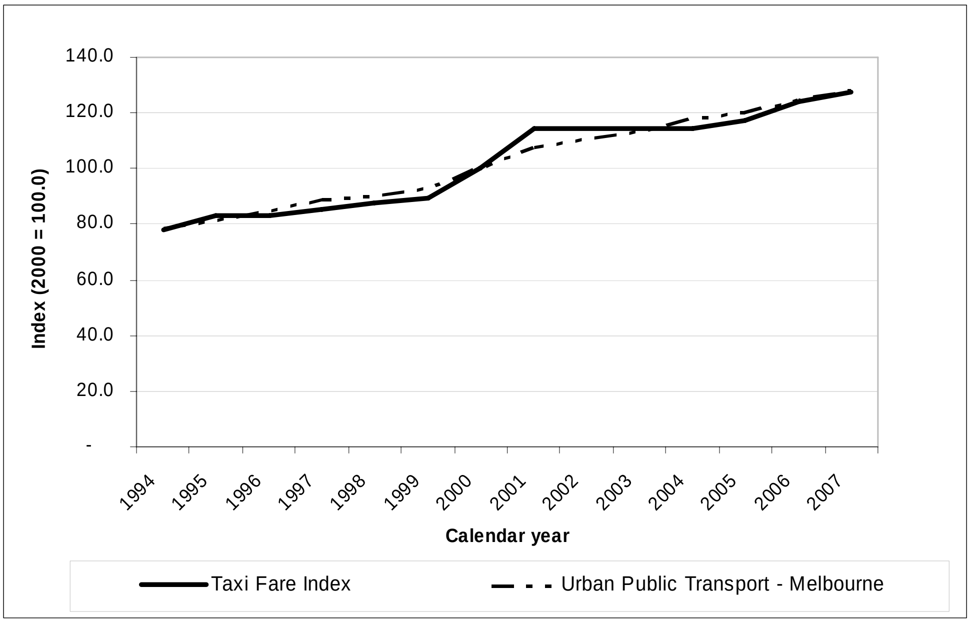
3.1 Benchmarking charges

Comparison with Trends in Urban Public Transport Fares

One of the closest substitutes for taxi services is public transport. Although many taxi trips will involve origins and/or destinations or times-of-use where there is no close public transport alternative, from a broad perspective, the taxi industry competes with public transport for a significant part of its business.

Figure 3.1 shows an index of taxi fares since 1994, together with the Australian Bureau of Statistics (**ABS**) index for urban public transport fares in Melbourne over the same period. The chart shows that over the period since 1994, taxi fare levels have increased at a similar overall rate to other public transport fares. This suggests that the competitive position of taxis versus its main competition has remained stable.

Figure 3.1 **Comparison of Taxi & Urban Public Transport Fares**



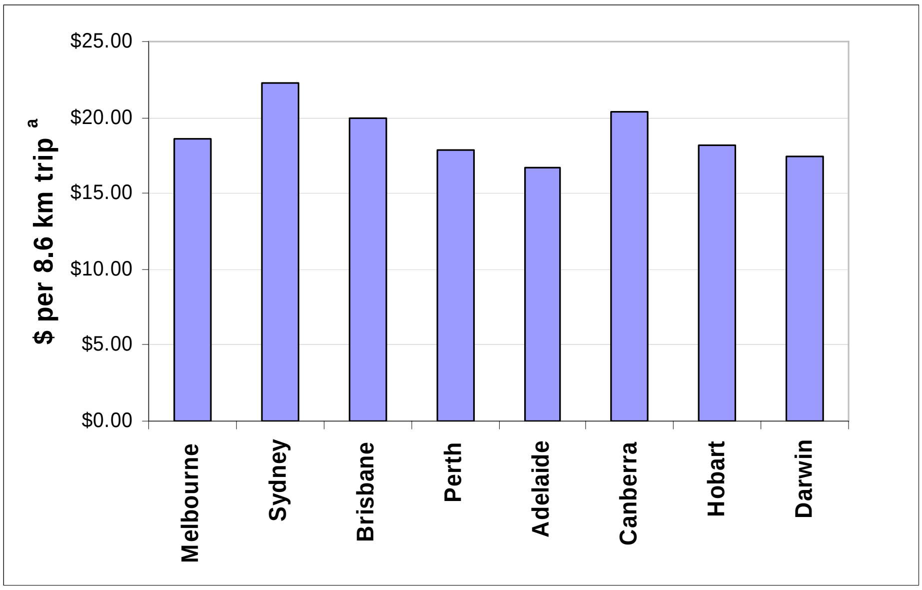
Data source: ABS Urban Public Transport component of the CPI, Melbourne, ESC constructed index of taxi fares based on announced fare movements

Benchmarking against other jurisdictions

A different approach to assessing the reasonableness of taxi fare levels is to benchmark prices against other jurisdictions. Comparisons of this kind have a number of drawbacks and limitations. In each capital city there are differences in the public transport systems, public transport fares, urban density, and a wide range of other factors that may affect the level of taxi services provided and the prices that may be charged. Nevertheless, these comparisons are of interest, and can be informative.

Figure 3.2 compares the fare calculated for an 8.6 kilometre trip during weekday daytime hours in Melbourne compared to capital cities in other states and territories. This comparison shows that the level of taxi fares in Melbourne is lower than in Sydney, Brisbane and Canberra, and at a higher level than Adelaide and Perth.

Figure 3.2 **Indicative Metropolitan Taxi Fare[a]**



[a] Assumes 8.6 km day-time / Tariff 1 trip, pre-booked, with 3 minutes waiting time (According to the Australian Taxi Association, *State & Territory Statistics as at December 2006*, 8.6km is the average job for a metropolitan taxi in Australia).

Data sources: VTD website; NSW Ministry of Transport[8]; Queensland Transport (provided by email); Taxi Council of WA[9]; Taxi Council South Australia[10]; ACT Territory and Municipal Services; Tasmanian Department of Infrastructure, Energy and Resources[11]; Northern Territory Transport Group[12]

Relevant differences between the capitals include number of trips per cab per year, average trip lengths, proportion of booked engagements. For example, in Sydney there is a much lower proportion of booked engagements than in Melbourne. The ATIA[13] estimates that 28% of taxi trips are booked in Sydney, compared to 50% in Melbourne. Other relevant differences include the number of cabs per head of population, licence rental costs and possibly differences in waiting times for users (although unlike Sydney, these are not currently available for Melbourne). For example, on a per capita basis there are 20-35% more taxi cabs in Sydney and Brisbane compared to Melbourne.

The markets therefore have different characteristics and in the absence of greater information on the elasticity of demand in Melbourne, and service levels compared

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8 http://www.transport.nsw.gov.au/taxi/fares.html

9 http://www.tcwa.com.au/servtaxifares.html

10 http://www.taxicouncilsa.com.au/taxi_fares_charges.htm

11 http://www.transport.tas.gov.au/pdf/misc/Paper20220-20Fares.pdf

12 http://www.nt.gov.au/transport/taxi/tariffs/index.shtml

13 Australian Taxi Industry Association, *State & Territory Statistics as at December 2006*

to other jurisdictions, it is not feasible to use such comparisons as a basis for making recommendations on taxi fare levels in Victoria. Observations on fare levels in other jurisdictions do not directly address the issues concerning the sustainability or affordability of services in Victoria.

Summary conclusions:

The relative competitive position of taxi fares against public transport fares appears to have remained stable.

Whilst benchmarking taxi fares against other states shows Melbourne fares are approximately 10% and 20% below Brisbane and Sydney respectively, the benchmarking results do not provide guidance on the appropriateness of taxi fare levels in Victoria with reference to efficient costs including a reasonable margin and effective levels of utilisation.

3.2 Survey-based estimates of costs and margins

Although the development of processes to improve data collection is being established as part of the Taxi-cab Industry Accreditation Regulations, at the time of undertaking this Review, data collection relating to industry revenue, costs and demand has not yet been carried out and the Commission has had to rely on surveys.

In its 2005 Taxi Fare Review the Commission engaged PricewaterhouseCoopers (**PwC**) to undertake a survey of various taxi industry participants to develop estimates of taxi operator costs for 2000 and 2004.

For the purposes of the present review the Commission engaged PwC to carry out a broad-based survey of taxi operators and drivers[14]. The operator survey was mailed to approximately 2,600 taxi operators in the metropolitan and regional areas, and the driver survey was mailed to approximately 4,100 drivers contracted through bailment agreements (that is, drivers who did not hold a taxi licence or operate one on assignment). In total 431 responses were received. This data has been analysed by PwC, and forms the basis of PwC's cost estimates for 2007. The PwC survey report is attached as Appendix C.

Table 3.1 summarises the PwC cost estimates from both the 2004 and 2007 studies. These cost estimates are representative of an 'average' Victorian taxi operator. Notably, however, taxi operations are small businesses with differing cost structures, for example, due to different approaches to maintenance, and different rates of taxi use. Hence the costs of individual operators may vary significantly from those of an average operator. PwC also notes (p.7) that at a 95% confidence interval the costs and revenue results could vary by up to 6.8%. Given the possibility of sampling error, the results of the survey need to be treated with caution.

[14] See Appendix C of the Issues Paper for examples of the questionnaires.

Table 3.1 **Estimated taxi operator costs ($ per taxi)**

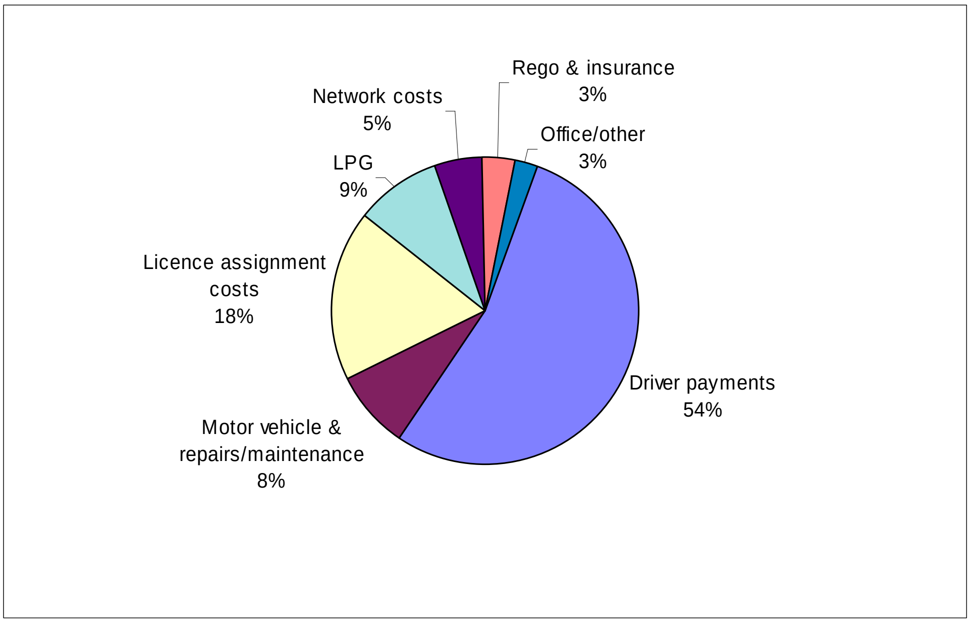
	2000	*2004*	*2007*
Driver payments	63,097	66,283	71,411
Vehicle lease payments/finance	5,923	5,397	6,653
Licence assignment fees	19,213	20,580	23,418
LPG	11,168	10,019	12,314
Network fees	5,144	5,831	6,739
Repairs/maintenance/tyres	5,307	6,236	4,441
Registration & insurance	4,056	5,003	4,274
Office & other	7,499	8,476	3,361
Total	121,407	127,825	132,611
Estimated revenue	126,194	132,566	142,823
Operator margin (% of costs)	3.9	3.7	7.7

Sources: Essential Services Commission (June 2005) *Final report: Taxi Fare Review 2005*, p.44 & p.37; PwC 2007 survey results

Note: The median Victorian taxi has been deemed the 'average'.

The relative importance of each of the main taxi operator costs are shown in Figure 3.3. For example, LPG costs were estimated to represent 9% of taxi operator costs in 2007, while licence assignment costs represented 18% of costs. Driver payments, estimated to be 50% of revenue, amount to more than 50% of costs because revenue exceeds costs.

Figure 3.3 **Breakdown of taxi operator costs 2007**



Data source: PwC 2007 survey results

Adjustment for licence assignment fees

In Figure 3.1, license assignment fees are the second largest component of costs after driver payments. An important methodological issue is whether licence assignment costs are to be included when calculating taxi costs and trends or whether they are to be regarded as a profit item with the rent being redistributed to taxi plate owners (see chapter 4 for further discussion of income distribution).

The increase in assignment fees in recent periods represents an increase in the capture of economic rents by licence holders from taxi operators and users. It has also been argued that these fees should decrease when taxi operator costs rise, as the available rents are reduced. Not only is it an economic rent, but the inclusion of increases in assignment fees as a cost for the purposes of determining fares would introduce a circularity (increases in assignment fees would generate higher fares, in turn resulting in higher assignment fees, and so on).

As such, it would not be appropriate, for the purposes of this assessment of fare adequacy, to include the recent increases in assignment fees in the cost base for the purpose of considering the sustainability of fare levels. Thus, in the calculation of taxi operator returns below, the 2004 assignment fee cost has been used.[15]

[15] Note that the Independent Competition and Regulatory Commission (ICRC) took a similar approach to the question of network fees in the ACT which it considered to be excessive. See ICRC (May 2004) 'Final Report: determination of taxi fares for the period 1 July 2004 to 30 June 2007', pp 27-30

Taxi operator returns

The taxi operator margin in 2007 averaged 7.7% over costs, as shown in Table 3.1. This margin has increased significantly since the 2000 to 2004 period. The 2004 PwC survey found that taxi operator returns represented 3.9% over costs in 2000 and 3.7% in 2004. Operator returns in 2007 would have been approximately 10% of costs in the absence of the increase in licence rental costs since 2004. This increase in margins appears to be largely due to the 8% fare increase in September 2007, only partly mitigated by increased LPG prices.

Licence holder returns (i.e. assignment fees) were over 15% of fare revenue in 2000 and 2004, increasing to 16.4% in 2007. The recent increase in licence assignment fees as a proportion of revenue is despite the increased relative importance of peak period cabs and WATs, with relatively lower licence rental costs.

The combined returns to operators and licence holders have increased from around 19% of fare revenue in 2000 and 2004, to 23.5% in 2007. Network fees have also increased over the period from 2004 to 2007 by approximately 5% on average per year.

Impact of recent LPG price movements on margins

The estimated impact of recent increases in the LPG price on taxi operator margins is shown in Table 3.2. For this table the PwC cost estimates for 2007 are interpreted as representing an average for the calendar year 2007, and provide the basis for the non-LPG costs assumed. Varying LPG prices are applied using the 2007 kilometres per cab. Thus the table shows changes in the estimated margins due solely to movements in the LPG price.

It is estimated that over the December quarter 2007 taxi operator margins will have averaged around 6.3%, and in January will have reduced to around 4.1%. However, with the reductions in LPG prices forecast by the Nymex futures market, the average taxi operator margin is expected to increase to an average of around 5.9% over the months of February to June. Excluding the increase in assignment fees from 2004 to 2007, this margin would amount to approximately 8%.

Table 3.2 **Estimated taxi operator margins** (% of costs)

	2007 average[a]	*Dec Qtr 2007*[b]	*Jan 2008*[b]	*F/C Feb-June 2008*[b]
Average LPG Price (cpl)	49.6	56.7	67.9	58.7
Estimated operator margin (%)	7.7	6.3	4.1	5.9
Adjusted operator margin[c] (%)	9.8	8.4	6.2	8.0

a PwC survey results. **b** All non-LPG costs assumed to be at their average 2007 level. **c** Excluding the increase in assignment fees between 2004 and 2007.

Sources: ESC estimates

Operating margins of 3-8% are considered to be common in trading businesses with low degrees of capital intensity. In NSW, where operator margins have been treated as a cost (‘operator salary equivalent’) rather than a margin as in the PwC analysis of taxi operator costs, these costs have been estimated to be just under $10,000 per annum.[16] On the basis of the estimated average revenue of a Victorian cab in 2007, this would be equivalent to an operator margin of approximately 7.5% per annum.

Summary conclusion:

An analysis by PwC of a broad-based survey of taxi operators and drivers in December 2007 has found that taxi operator margins have increased from less than 4% in 2000 and 2004, based on PwC’s previous survey, to approximately 8% in 2007, which appears to be adequate and reasonable for a trading business of this kind. This result needs to be considered in light of the degree of confidence attributable to the survey results.

This margin would have been approximately 10% in 2007 absent an increase in licence rental fees from around 15% to 16.4% of revenue over the same period. Utilising the PwC analysis, over the coming months taxi operator margins can be expected to be slightly lower than the 2007 average, perhaps around 6%, which would be equivalent to 8% with licence assignment fees at the 2004 level.

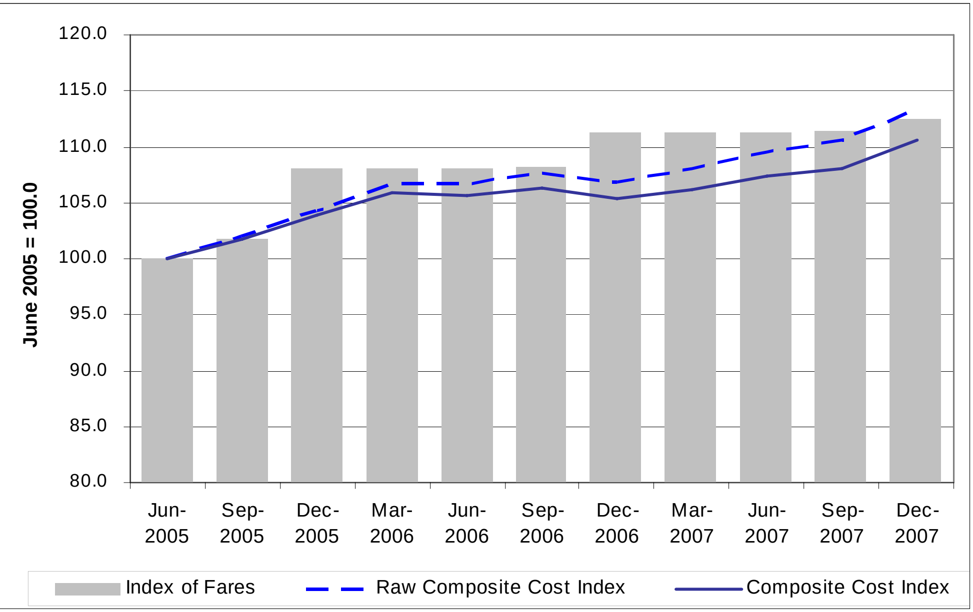
This is not as high as margins of around 8-10% that were expected to follow from the 8% fare increase in September 2005.

3.3 Tracking Costs over time

Trends in fare levels can also be compared to indices of unit costs. Figure 3.4 shows an index of taxi fares over the period from June 2005 to December 2007. This is compared to a composite index of input prices. The input price index is also adjusted to take into account an assumed productivity growth of 1% per annum to provide an estimate of unit costs. The assumed 1% productivity growth is based on the Commission’s approach for the previous taxi fare review. For the Draft and Final Report, the Commission would investigate further the size of the productivity gains experienced by the industry.

[16] See: PricewaterhouseCoopers (January 2008) ‘Ministry of Transport: Review of Weightings in Taxi Cost Model’, p.22.

Figure 3.4 **Index of fares & estimated costs Jun 2005-Dec 2007** (assuming 1% productivity gain p.a.)



Sources: Fare data: ESC 2005 and VTD 2007; CPI & AWE (ordinary time earnings): ABS 2007 6302.0 & 6401.0

The assumed composite input price index has been constructed using the following indices from published sources: the ABS Labour Cost or Wage Price Index (**WPI**) (used as the input price index for driver incomes); the Private Motoring Index (**PMI**) in the CPI, Melbourne (used as the input price index for motor vehicles, repairs and maintenance, tyres and washing and other on-road costs); FuelTrac reported LPG retail prices; the Insurance Index in the CPI, Melbourne; the CPI – All Groups, Melbourne (used for network fees, office, uniform and other costs). These indices have been weighted by the cost shares in the 2004 PwC survey. Appendix B contains more information on how the composite input price index has been calculated.

Figure 3.4 shows show that over the recent period fare level trends have, broadly speaking, been similar to the increases in unit costs. However, it is also consistent with a reduction of margins from around 8-10% expected following the 8% fare increase in September 2005, to around 8% by June 2008. As the input price and unit cost indices do not include licence assignment fees, the escalation of licence rental costs will have represented an additional source of burden to taxi operators, but the Commission regards assignment fees as a matter relating to the distribution of the total taxi industry income between industry participants. As such, it is not included in the composite input price index.

Figure 3.4 indicates that the increase in costs was 10.6% between the June quarter 2005 and the December quarter 2007. Taxi fares increased by 12.5% over the same period, taking into account the 8% increase in September 2005. Figure

3.4 also depicts the recent pressure of costs impacting especially on the December quarter 2007.

The constructed composite input price index also readily allows the impact of increases in LPG prices to be estimated. The contribution of increased LPG prices to the increase in the index has been 3.8% in total over the period from the June quarter 2005 to the December quarter 2007.[17] The average LPG price in the December quarter 2007 was 56.7 cpl - a similar level to the forecast for LPG prices from February to June 2008 shown in Table 3.2. It is estimated that if taxi fares were increased by 3.8%, the forecast taxi operator margins in the period February to June 2008, based on the analysis and assumptions used in Table 3.2, would be approximately 7.8% (based on 2007 costs including assignment fees, but using Nymex futures to estimate LPG prices over that period). This would represent a margin of approximately 10% if licence assignment fees were at their 2004 level.

Summary conclusions:

Unit cost increases measured by the composite input price index adjusted for productivity improvements, have broadly kept pace with fare increases over the period from 2005 to 2007.

This is consistent with a reduction of margins from around 8-10% expected following the 8% fare increase in September 2005, to around 8% estimated by PwC in 2007.

The trends of recent months are also consistent with an erosion of margins to slightly lower levels in December 2007 compared to the 2007 average.

The increase in LPG prices is estimated to have contributed 3.8% of the increase in the input price index since June 2005.

3.4 Conclusions on cost movements since the last review

The question that has been addressed in this chapter is the adequacy of prevailing taxi fare levels in light of costs, including LPG prices. This analysis has been informed by a survey of taxi operators carried out on behalf of the Commission by PwC, and a consideration of trends in unit costs derived from published indices.

The findings of the survey relate to the 2007 calendar year. They suggest that taxi operators were achieving higher margins during 2007 than was the case at the time the 2005 fare review was conducted, and the 2007 level of margins appear to be at a reasonable level (for example, when compared to the ‘operator salary equivalent’ estimated by PwC for NSW). However, they are lower than the 8-10% level expected following the 2005 “catch up” fare increase in September 2005.

The analysis shows that these margins have, over recent months, been squeezed by LPG prices and licence assignment costs. However, when the increases in

[17] This is the percentage difference between the composite input price index in December 2007 and the value that the composite input price index would have been in the absence of any increase in LPG prices from June 2005. See Appendix B for more information.

licence assignment costs are excluded, and the outlook for reduced LPG prices as indicated by the Nymex futures market is taken into account, the average taxi operator margins are expected to remain in an acceptable range over coming months. Excluding assignment fee increases, an 8% taxi operator margin is projected to June 2008. In summary, the survey finds that operator margins still remain within a commercial range. LPG prices are not expected to impose a sustained pressure on taxi operator margins, given the market forecasts for price reductions over the coming months. The degree of confidence that can be placed in the survey-based estimates is limited by the sample size.

A composite input price index has been constructed which shows that since the time of the September 2005 price increase, input prices (excluding licence rental) have increased at a faster rate than CPI, primarily due to increases in the prices of LPG. The adequacy of prevailing taxi operator margins appears to be primarily due to the 8% fare rise in September 2005, which has only been partly offset by increases in LPG prices and licence assignment fees.

However, while it can be argued that these projected margins could be sustained until fares are determined later this year, the cost increases due to LPG prices were not anticipated in 2005 when the prevailing price path was put in place and as a consequence the margins have reduced markedly. Furthermore, a degree of care needs to be taken in relying on survey results as an accurate predictor of actual margins because of the sample size[18].

The Commission is mindful that the increases in LPG prices have not been explicitly accommodated within the current pricing formula. The analysis indicates that LPG prices have added 3.8% to costs between the June quarter 2005 and the December quarter 2007, and an increase in fares of this magnitude would still leave taxi operator margins within the reasonable range. It can be argued that the increase in LPG prices is an unforeseen outcome under the existing fare escalation formula. Taxi industry accreditation is also estimated to add a small margin to costs – approximately 0.3% per annum.[19] Together these two unforseen additional costs are estimated to represent an increase in costs of approximately 4% in total.

[18] PwC notes (p.7) that at a 95% confidence interval the costs and revenue results could vary by up to 6.8%.

[19] Derived from: The Allen Consulting Group (October 200&) ‘Transport (Taxi-Cab Industry Regulations 2007: Regulatory Impact Statement’, p.x. The estimated net present value of all costs to the taxi industry as a whole associated with the regulations is $17.7m, using a 3.5% discount rate over a 10 year period. This implies a levelised annual cost of $0.6m, or approximately $130 per annum for each of the 4,651 taxi cabs.

4 IMPACTS ON USERS

The terms of reference require the Commission to have regard to the impact of a taxi fare increase on:

- Victorian business and the community, and the availability and affordability of services to customers, and
- taxi industry participants including licence holders, taxi operators, drivers and employees.

Section 4.1 discusses the interests of disadvantaged taxi users, and section 4.2 describes the potential effects of a fare rise on industry participants.

4.1 Users

PwC's survey analysis indicates that the median total kilometres (paid and unpaid) per cab was 116,000 in 2007 – of which 50% of kilometres were paid. The Commission's best estimate of the total market growth of taxi services is approximately 1.0% per annum on average between 2000 and 2007.[20] Hence the taxi market has not shown strong underlying growth in recent years. Taxis appear to have lost mode share in the passenger transport market.

Disadvantaged users

Taxis are an important mode of transport for specific community groups. For example, the elderly and people with disabilities often rely on taxis. It is estimated that 19% of taxi users are pensioners or retirees. Over 20% of these use a taxi more than once a week. Approximately 10% of taxi users are estimated to be members of the Multi-Purpose Taxi Program (**MPTP**) – a subsidy scheme for people with a permanent or severe disability who must rely on taxis.

In its submission VCOSS notes the importance of 'the ongoing ability of the taxi industry to continue to improve service coverage and quality for low income and disadvantaged Victorians'[21], but also highlights that:

> *From a taxi user perspective, a pricing model which will lead to rapid or substantial increases in taxi prices will have negative financial and social impacts. People that are dependent on fixed*

[20] This estimate has been derived by deflating the surveyed revenue estimates for 2000, 2004 and 2007 by an index of taxi fares (based on announced fare rises), and multiplying the resulting index of the quantity of services provided per cab by the number of licences on issue in each of those years.

[21] VCOSS submission, p.3

> *incomes such as government pensions are particularly vulnerable to price rises. Pensions are linked to CPI …*[22]

The Department of Human Services (**DHS**) submission also raises concerns about affordability, particularly for the MPTP users, and especially in country areas.

Preliminary conclusions:

Observations made by submitters concerning the impact of price increases on certain users suggest that price rises should be moderate and predictable.

However, affordability of taxi services needs to be balanced against the availability of taxi services on a sustainable basis.

4.2 Impacts on industry participants

The impact of a price increase on the taxi industry participants is largely associated with the impact on revenue. A decrease in demand due to increased fares would mitigate the improvement in revenue but may also reduce on-road costs by reducing the engaged kilometres driven. This cost reduction would be relatively small against the overall increase in revenue associated with a price increase.

Effect of fare rise on industry revenue

The increase in revenue resulting from a price increase depends on the elasticity of demand. There is very little information on the elasticity of demand for Victorian taxi services at the present time.

In other jurisdictions:

- research on taxi demand elasticity in the ACT carried by Booz Allen Hamilton found an average taxi demand elasticity of –0.36, which was broken down into a peak period elasticity of –0.23 and an off-peak elasticity of –0.41. [23]
- advice to IPART by Booz Allen reported that overseas studies have found the taxi demand elasticity may be around –0.8.[24] However, Booz Allen considered that in Australia demand may be less elastic. Based on its review of international studies, and considerations specific to Australia, Booz Allen concluded that the demand elasticity is likely to be in the range –0.3 to –0.8.

The VTA has commented on these estimates:

> *The elasticity estimates reported in the Booz Allen Hamilton IPART report range from -0.3 to -1.4 with a preferred estimate in the range*

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[22] VCOSS submission, p.4

[23] Booz Allen (April 2003), 'Final Report: ACT Transport Demand Elasticities Study', Department of Urban Services, p.34

[24] Booz Allen Hamilton (July 2003) p.11

-0.3 to -0.8. This range is so large that it is almost useless for forecasting the impact of fare changes on revenue[25]

Moreover, the demand elasticity for taxis may vary from city to city depending, in part, on the relative degree of competition between public transport and taxi services. For this reason the taxi demand elasticity studies prepared for the ACT and NSW may not provide a useful guide to the Melbourne market. For example, in Melbourne, taxi services face a high degree of competition from hire car services, particularly in the corporate and tourist markets.

Different market segments, such as private household demand, tourists, and corporate users are believed to have different degrees of price responsiveness. Private or social demand users are sometimes considered to be the most price-sensitive part of the market. For example, in its study of the ACT transport market, Booz Allen found the elasticity for taxi users not charging fares to a third party (i.e. broadly non-corporate) to be −1.4.[26], that is, price sensitive. In Victoria, the corporate and tourist market segments may also have a relatively greater price sensitivity than in some other jurisdictions due to vigorous competition from hire cars.

Distribution of revenue between industry participants

In Victoria approximately 90% of all non-operator drivers are engaged under a revenue sharing arrangement in which they receive around 50% of fare revenue, and typically do not pay for fuel costs. Only a small proportion use fixed pay-in arrangements. For this reason, approximately 50% of the increase in revenue from a price increase will be received as income by drivers (and operators in their role as drivers). The percentage increase in driver incomes would be similar to the percentage increase in revenue.

Depots/networks receive network fees from taxi operators. These fees are believed to be largely a fixed cost, and may not increase in response to a fare increase in the short term. However, this is uncertain. Network fees increased following consolidation of the networks now affiliated with Black Cabs, and the PwC 2007 survey shows that network fees have continued to increase at an average annual rate of approximately 5% between 2004 and 2007. In the longer term, although taxi operators can switch between depots, there is very little choice regarding marketing in any given locality. Hence there is a risk that network fees may increase to capture economic rent.

Licence holders receive assignment fees from taxi operators for the rental of licences. Due to the scarcity of the licences, these fees tend to increase to the maximum amount that taxi operators will bear.

Taxi operators retain the revenues not allocated to drivers and pay for the costs of operating and maintaining the taxis, as well as network fees and licence assignment fees. Due to the large number of potential taxi operators compared to

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[25] VTA submission, p.12

[26] Booz Allen Hamilton (July 2003) *Appraisal of Taxi Fare Structure Issues*, prepared for IPART, p.13

the constraint licence supply, the earnings of taxi operators tends to be driven down toward the level they would earn as bailee drivers. Some former cab operators have indicated they shifted to working as drivers for this reason.

The market for renting licenses

As discussed in chapter 2, recent increases in licence assignment costs are a significant source of higher costs in addition to LPG prices. Competition between prospective taxi operators for use of the scarce licenses determines the assignment fee (the market value of licenses being the capital value of expected future assignment fees). The competition between prospective operators for licenses ensures that the licence assignment fee captures the economic rents, leaving operators with a modest return (i.e. they have competed this away in bidding for the licenses). This "scarcity rent" to the licence holder can be viewed as a profit item in the industry rather than a cost of operating.

The submission from Mr Walsh stated:

> *The fact that licences have a value greater than zero is evidence of two truths:*
>
> *a) There are too few licences (supply and demand)*
>
> *b) Super profits exist in the present level of fares. i.e. If fares were at the correct level to give a fair compensation for the cost of investment in and operation of the vehicle, remuneration per hour for the driver and cover for overhead expenses, there would be no funds available to pay for rent of a licence, and therefore licences would have no value.*

The submission of Mr David Griffiths observes:

> *It can be clearly seen from your issues paper that the investors* [in licences] *are a dead weight to this industry*

The Commission has previously observed that there may be an imbalance of market power in the market for licence assignment:

> *Similarly, there is some evidence, beyond that cited above in relation to rate of return, to suggest that operators also find themselves in a poor position in negotiations with licence owners in regard to assignment contracts. In an efficient market, operators struggling to earn adequate returns would be expected to exert pressure on licence holders to reduce their assignment fees or to remove restrictive clauses, such as automatic escalation in line with CPI or fare increases. This does not appear to be happening and may be a product of the fact that most operators are very small-scale businesses and, hence, in a position of limited bargaining power in respect of assignments.*[27]

[27] 2005 Taxi Fare Review: Final Report, p.46

Summary impacts on industry participants

Given this process, it is reasonable to expect that very little of any fare increase will be retained by taxi operators, for reasons already explained in relation to the market for taxi licences. Most likely this revenue will be captured by licence holders through higher assignment fees than would otherwise be the case. However, given the high degree of concentration among depots/networks, and it is possible that some of the increase in revenue will flow to the depots/networks through higher network fees.

It is also possible that driver incomes will not increase as much as expected, if the standard bailment arrangements are modified to reduce the effective driver share of revenue. In summary, with respect to the question of a price increase, taxi drivers may be beneficiaries through income sharing arrangements, while licence holders and possibly depots can be expected to benefit by having greater ability to push assignment fees and/or network fees higher. Taxi operators may not obtain much benefit if assignment fees increase further in response to the fare increase.

Thus although the licence assignment market has seen some reductions in licence assignment fees occurring in February 2008, fare increases are likely to reduce the pressures currently applying in the licence assignment market rather than flowing through to operators.2008. Hence licence holders are considered to be key beneficiaries of any fare increase.

The high current value of licences suggests that consideration of whether further relaxation of supply constraints to expand the release program would be beneficial will be a relevant issue to examine in the Draft Report and report on in the Final Report. Currently the main source of current licence growth is the “Green Top” program, releasing 100 extra plates per annum (or approximately 2.2% of the fleet), with 500 of these licences issued to date. These cabs are limited to operating between 3 pm and 7 am (i.e. a single shift every 24 hours), as well as certain major events. The Victorian government is committed to issuing a further 100 of these licences, and converting at least 50% of these licences to full licences on the sixth anniversary of their issue date. By enabling these cabs to operate additional shifts, this will add to the supply of cabs. The Government has also stated that industry performance monitoring will determine whether there is a need to increase the number of licenses further.

Preliminary conclusions:

Driver incomes (and the incomes of operators in their capacity as drivers) would increase proportionately to industry revenue under current bailment arrangements in which drivers typically retain around 50% of revenue. However, given the relatively weaker bargaining position of drivers, there is a risk that drivers may not achieve all of this gain if bailment arrangements change.

Taxi operators cannot be expected to gain significantly from a price rise.

In the current highly concentrated market, there is reason for concern that the main impact of a price rise on industry participants will be to enhance the returns for the segments of the industry with market power, namely the

licence holders and the depot/networks. Given the high licence values, the effectiveness of the licence release program is an issue for consideration in the Draft and Final Reports.

5 COUNTRY TAXI FARE LEVELS

By way of their charge as ‘common carriers’, whereby taxis are required to serve passengers on demand, taxis form part of the public transport system. This responsibility is particularly pronounced in regional Victoria, given the limited supply of train, tram and bus services in the country. In many instances, taxis represent the sole form of public transport within the community. For this reason, special regard must be given to country taxi operations.

This chapter examines the adequacy of the level of country taxi fares. This issue is being addressed separately in this Interim Report because previous reviews have raised specific concerns about the financial viability of taxi services in small county towns. In the 2005 Taxi Fare Review, concerns were raised by a number of submitters, and the Commission concluded that a detailed examination of this issue was warranted. This Interim Report contains a preliminary analysis.

5.1 Relativity between Metropolitan and Country Fares

In the current Victorian fare structure, higher distance rates are charged for regional and country taxi services than for metro services. ‘Regional services’ refers to Geelong, Ballarat and Bendigo. ‘Country services’ refers to all other Victorian towns with taxi services.

Table 5.1 shows the fare calculated for a 10 kilometre trip during weekday daytime hours in each jurisdiction and region. Victorian country taxi fares are approximately 5.4% higher than metro fares when using a 10km trip for comparison. This relativity is broadly similar to NSW, but is a smaller fare differential than in some other states.

Table 5.1 **Average Fare for 10 km trip**

Jurisdiction	***Metro***	***Regional***	***Country***	***% diff. Regional & Metro***	***% diff. Country & Metro***
Victoria	$20.63	$21.34	$21.75	3.4	5.4
NSW	$24.81	-	$25.76	-	3.8
QLD	$22.26	$23.06	$32.46	3.6	45.8
WA	$20.23	-	$28.53	-	41.0
SA	$18.71	-	$21.71	-	16.0
Tasmania	$22.65	-	-	-	-
NT	$20.38	$20.38	$21.34	0.0	4.7

Note: Assumes a booked taxi service based on day-time rates with 3 minutes waiting time. Tasmania and NT regional and country fares are comprised of averaged values for Flagfall, Distance and Waiting Time. Tasmania regional is deemed to include Launceston, Devonport and Burnie. Tasmania country is deemed to include King Island and Flinders Island and any other area not in Hobart or regional. NT regional is deemed to include Alice Springs and Katherine. NT Country is deemed to include Nhulunbuy and Tennant Creek.

5.2 Cost comparison between Metropolitan and Country Zones

The cost pressures facing country taxi operators are markedly different from their metropolitan counterparts – as shown in Table 5.2. PwC’s analysis of the 2007 survey responses indicates that the total annual costs for an average country taxi are similar to the costs for a metropolitan taxi. However, the country taxi is typically obtaining lower revenue than a metropolitan cab (due to lower trip volumes and often shorter distance trips), notwithstanding the higher fare in country areas.

Table 5.2 **Taxi Operator Costs – Metro & Country ($ per taxi)**

	Metro [a]	***Regional*** [a]	***Country*** [a]
Driver payments	71,617	76,830	67,080
Vehicle lease payments	6,648	6,652	6,688
Licence assignment fees	24,055	15,340	22,412
LPG	12,096	12,365	14,144
Network fees	6,247	10,000	9,000
Repairs/maintenance/tyres	4,257	5,929	5,659
Registration & insurance	4,479	3,750	2,916
Office & other	3,208	3,195	4,650
Total Cost	132,591	133,051	132,549
Revenue	143,235	153,660	134,160
Operator margin	8%	15%	1%

a "Metro" here refers to the Metropolitan and Outer Urban zones; the "Regional" zone encompasses Geelong, Ballarat and Bendigo; while "Country" refers to all other cities and towns with taxi services in Victoria.

Source: PwC 2007 survey results

Comparing the costs of country and metro cab operators derived from the PwC survey, some of the main findings were:

- Contrary to the usual assumption, taxi licence costs reported to the survey for country operators were found to be broadly similar to metro levels. This is discussed further below.
- Overall some services are cheaper outside of Melbourne – such as insurance
- Other costs such as network and administration costs are somewhat higher, suggesting economies of scale in fleet management costs and overheads. Repairs/maintenance/tyres are also higher, possibly due to transport costs from the CBD or due to there being less choice of provider.

Although country taxis are also usually believed to cover considerably less paid kilometres than metro cabs, the PwC survey did not bear this out. Fare revenue per cab was found to be higher in the major regional centres (i.e. Geelong, Ballarat and Bendigo), but in other country areas they were approximately 7% lower than for metro cabs. Drivers obtain a correspondingly lower income.

Taxi operators participating in the survey were found to obtain a much lower operating margin in country areas – on average only 1%, compared to 8% in metro areas. On the other hand, the PwC survey found taxi operator margins in the major regional centres to be higher.

The finding that taxi operator margins in country areas are small needs to be considered against the observation that in country areas 'the majority of taxis are operated by the Licence Holder – country taxis are typically not assigned to a third party'[28]. Thus the 'licence assignment fees' in this case are actually returns to the taxi operator. These taxi operators will usually have invested in their licence, but it is not possible to separate the return on the licence and the return to the taxi operations. This appears to be the reason why licence fees appear to be surprisingly high in the country and operating margins low. They have in effect been consolidated under the heading 'licence assignment fees'.[29]

Table 5.2 shows that for the average country cab, the combined licence assignment fee and operator margin as a percent of revenue was over 18% in 2007.

As previously mentioned, in the metropolitan market, the market value of licence assignment fees should adjust to absorb or reflect changes in the cost base of operators. This process will ensure that licences are always assigned and that the supply of taxis would not be reduced when an operator exits the market. However, the same mechanism may not be active in all country locations, particularly as country taxi cab operators are also typically the licence holder. There is a greater risk that a scaling back of operations, or the exit of an operator entirely, could reduce the availability of taxi services. Additionally, some country towns have fewer employment opportunities and in some cases people have purchased taxi plates and then undertaken driving services as a means of obtaining rural employment whilst at the same time procuring a tangible asset.

The 2006 Country Taxi Review expressed concern about the financial viability of operators in rural and regional Victoria in towns where small population sizes (and thus limited demand) have an impact on operating revenue. The Country Taxi Review calculated that the minimum population size required to generate sufficient returns to operators was 2,500. On this basis, the Country Taxi Review concluded that 34 towns served by taxis fell below this threshold, and that the firms operating in those communities would likely be financially marginal. Were those towns to lose their taxi operators, it is improbable that they would be replaced. As such, the risk that such communities might not have any form of public transport must be a concern. Relevant options will be considered in the Draft and Final reports of this Review.

5.3 The impact on users of service availability

While the viability of regional taxi operations is an important consideration, the impacts of a significant fare increase for regional taxi services will impact on taxi users and in some localities may result in a reduction in total fare revenue

The market for taxi services in regional areas differs in the function that taxis perform and the regulatory framework that is appropriate. There is a relatively greater degree of dependency on taxi use by some users without other forms of

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28 Victorian Country Taxi Industry Review Working Group (May 2006) 'Final Report: Country Taxi Review', p.7

29 This view is supported by presentations at the Bendigo public forum on 19 February 2008, at which information was presented on taxi operator costs for a country operator.

transport available. Furthermore, the Country Taxi Review found that 24% of country taxi users are MPTP members.

The DHS submission indicated that the MPTP segment of the market needs to be considered, especially in country areas, and the affordability of services given consideration.

On the other hand, the VTA has emphasised that:

> *The issue is not to force the taxi industry to provide a special deal for country people based on special needs. Welfare-related issues are best addressed by State Government policy. The primary issue is to make fare relativities reflect cost relativities in the different locations.*[30]

5.4 Conclusions

The prevailing returns to country taxi operators needs to be considered in light of the surprisingly high levels of licence assignment fees and the relatively low margins, in the context where taxi operators in country areas are also typically the licence holder.

The economic situation of country taxi cab operations needs further examination, and this will be undertaken as part of the Review and the Commission will provide further considered conclusions in its Final Report. If an interim fare increase is not made, and it is found that there are shortcomings in the returns of country taxi operators, then there is the possibility of a catch-up rise in September 2008. Other options to alleviate cost pressures or improve revenue generation for country taxi operators will also be considered in the Final Report.

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[30] VTA submission, p.12

6 RECOMMENDATIONS & PRELIMINARY VIEWS

Essentially the task for this Interim Report is to assess the impact and materiality of current cost pressures in the industry (with a focus on LPG) and potentially to identify options for addressing pressures. Primarily this includes the specific question as to whether there should be an interim price rise (and if so the amount of that increase) or, if there is to be a fare adjustment for these recent cost rises, whether it is better deferred until the planned annual fare rise in September 2008. Included within this question is whether a price increase is warranted in the metropolitan (including Outer Suburban) area or in the country and regional areas. The Commission's recommendations on each of these matters are set out in section 7.1.

Within this context it is also pertinent for the Commission to outline its preliminary views in relation to the formula for resetting prices from year-to-year, and in particular how any longer-term movements in LPG prices would be addressed within the fare adjustment mechanism. The Commission's preliminary views are outlined in section 7.2, including its position on VTA's proposed Fuel Price Levy.

The Commission also considers it to be useful to discuss some of the options it will consider in this Review that are relevant to improving driver remuneration, or addressing certain cost pressures in the industry, as well as addressing issues in relation to the viability of taxi operations in smaller towns. These matters are discussed in section 7.3.

6.1 Recommendation in relation to an interim price rise

Impact of LPG prices

Although LPG prices have increased strongly in December 2007 and January 2008, this is likely to be part of a seasonal pattern of summer peaks associated with the northern hemisphere winter heating demand for LPG. The latest bulk LPG benchmark contract prices indicate a price decrease of approximately 8%, and Nymex futures contracts indicate a market expectation of further reduction in LPG prices over the period from March to June 2008. Hence the cost pressure associated with LPG prices over the Australian summer happens in most years, and is likely to dissipate over the autumn period.

LPG prices are estimated to have increased taxi operator costs by 3.8% between June 2005 and September 2007. As the average level of LPG prices forecast for the period February to June 2008 is similar to their average level over the December quarter 2007, the estimate of 3.8% higher unit costs due to LPG prices is also the estimated impact of LPG prices in the near term.

The findings of a broad-based survey of taxi operators and drivers carried out on behalf of the Commission by PwC indicate that taxi operator margins have improved in 2007 towards adequate levels compared to previous survey results for 2000 and 2004, and the available evidence indicates that over the next six months, taxi operator margins are likely to remain within an adequate range, although these are not at the 8-10% levels anticipated at the time of the "catch up" price increase in September 2005.

Part of the increased costs for taxi operators has been the ongoing increases in licence assignments fees. The Commission's view is that this is largely a matter of the distribution of total taxi industry income between industry participants, and should not represent a basis for increasing taxi fares to the public.

Nevertheless, the Commission recognises that taxi operator costs have increased more rapidly than was anticipated in 2005, even without the increases in licence assignment fees is being taken into account. An interim fare adjustment would provide an immediate response to the impact of LPG prices on taxi operator margins.

On the other hand, the market for taxi licence assignments should ensure that upward pressures in taxi operator costs are accommodated by reductions in licence assignment fees. Although a clear trend to reduced licence assignment fees has been slow to materialise, there is some evidence of reductions emerging in February assignments. A fare increase may simply relieve the downward pressure otherwise applying on the licence assignment rates, and hence taxi operators may not benefit fully – licence holders can be expected to obtain some of the benefits.

There is also a risk in relation to the response of patronage to a fare increase. There is very little research available on the demand elasticity for taxi services. Features of the Victorian taxi market, including the degree of competition from hire cars and from tram services, means there is a risk that demand is price sensitive. This is reinforced by the very slow growth observed in the Victorian taxi market, when compared to the overall passenger transportation market. If patronage revenue is price sensitive then taxi drivers will be made worse off by a fare increase – as their income is generally based on a share of revenue.

Summary – impact of LPG prices

The Commission's estimate of the impact of LPG prices on operating costs is 3.8% between the June quarter 2005 and the December quarter 2007, and when accreditation compliance costs are included, which are estimated to add a further 0.3% to total costs, the Commission's estimate of the required catch up fare increase at the present time is approximately 4%.

Need for an interim fare increase

The Commission has been asked to advise whether an interim fare increase is warranted. These cost increases were not anticipated in 2005, and as such, operator margins are somewhat lower than expected when the prevailing price path was put in place. This is a matter that the Commission would consider in making its final recommendations in June 2008. However, an interim fare adjustment would provide an immediate response to the impact of LPG prices on taxi operator margins.

Taking the impact of LPG prices and the accreditation compliance costs together, the Commission's estimate of the required catch up fare increase at the present time is approximately 4%.

In its reviews the Commission has emphasised that the distribution of income within the taxi industry should be treated as a separate matter to setting taxi fare levels. Therefore, distributional considerations should not affect the quantum of any fare increase.

Nevertheless, a key concern of the Commission is the likely capture of any fare increase by licence holders, and possibly depots/networks, whereby fees payable by operators are increased commensurately. This would simply result in taxi users facing higher charges (and possibly reducing their levels of patronage), higher returns to licence holders and taxi operators getting little of the intended benefit. Given the turnover rates of existing assignment contracts (which have an average term of approximately one and a half years) this form of flow-through may be relatively moderate over the few months prior to the Commission completing its Final Report to the Review, which will address issues relevant to the distribution of income in the taxi industry.

Another concern is the extent to which any revenue increase flowing from an interim fare increase is likely to flow to taxi operators, who incur LPG costs. Under existing bailment arrangements 50% of any revenue gain would flow to operators and 50% to drivers. However, it is also observed in chapter 4 that drivers are in a relatively weak bargaining position, and that bailment terms may alter. Given this, the Commission has concluded in chapter 4 that there is a risk that drivers may not achieve all of this gain if bailment arrangements change. Taxi operators therefore may be the primary beneficiaries of a fare increase in the short term, but given the tendency for rents to flow through to assignment fees under current market and regulatory arrangements, taxi operators cannot be expected to retain those gains over time.

Given this assessment there does not appear to be a strong benefit, in the short-term, to options designed to 'quarantine' any revenue gains from a fare rise to taxi operators. Ensuring that any revenue increase flows only to taxi operators would either require direct controls over bailment contracts or licence assignment fees – in each case a significant intervention – or a form of levy that is not captured by the provisions in existing bailment or assignment agreements which may otherwise pass through part of any increase in revenue to drivers or licence holders.

As discussed in section 6.3 increased regulatory controls are only one approach to addressing the wider issues in relation to income distribution in the industry which the Commission will examine as part of the Review. A comprehensive review of the options for improving taxi operator and driver remuneration will be covered in the Draft and Final Reports of this Review.

On the question of whether a levy can be structured to 'quarantine' gains to taxi operators, one approach that has been flagged by stakeholders is the option of an 'off meter' levy. This approach would have the benefit of removing the need for adjustment of taxi meters (thereby avoiding the cost of doing so), but has a number of drawbacks in terms of lack of transparency, increased administrative costs of manual settlement transactions, and greater costs of handling of customer complaints by taxi drivers and relevant bodies. Instead, the Commission recommends that the cost of adjusting a taxi meter (estimated to be $140 by industry participants), be factored into any interim fare increase, and that any fare increase be 'on meter'. The Commission estimates the recovery, over a six month period, of the cost of adjusting a taxi meter would represent 0.2% of revenue based on PwC's estimate of the annual revenue for a median taxi cab. Therefore, the required fare increase would be 4.2%.

In relation to the potential demand response to an interim price increase, the Commission will give consideration in the Draft and Final reports to the benefits of a maximum fare regime in the pre-booked market, which may enable taxi operators to mitigate risks of a potential demand response by discounting fares, if this is found to be necessary or advantageous.

Other options to alleviate cost pressures or improve the ability to increase revenue will also be considered in the Draft and Final reports. This includes the impacts that increasing assignment fees can have on the ability of the industry to compete and provide high service standards.

Summary – required 'catch-up' fare increase

Although the broader question of fare adjustment is a matter that the Commission will consider in making its final recommendations in June 2008, an interim fare adjustment would provide an immediate response to the impact of LPG prices on taxi operator margins.

Taking the impact of LPG prices and the accreditation compliance costs, together with the costs of meter adjustment, the Commission's estimate of the required 'catch up' fare increase at the present time is approximately 4.2%. If an interim fare increase is to be made, this is the Commission's recommendation as to the amount of the fare adjustment.

Recommendation:

The terms of reference direct the Commission to assess the impact of sustained increases in LPG prices. The Commission has estimated that LPG costs have added 3.8% to taxi operator costs between the June quarter 2005 and the December quarter 2007. As the December quarter 2007 average LPG price is found to be representative of LPG prices in coming months, the 3.8% additional cost is also an estimate of the sustained impact of LPG prices on taxi operator costs.

The Commission is also directed to advise whether an interim fare increase is warranted. Some of the of cost increases due to rising LPG prices were not anticipated in 2005 when the prevailing price path was put in place. An interim fare adjustment would provide an immediate response to the impact of LPG prices on taxi operator margins. The Commission's best estimate, at the present time, of the required catch up fare increase is approximately 4%, taking into account the compliance costs associated with industry accreditation. An interim fare increase should be 'on meter' and include an additional 0.2% to enable recovery of meter adjustment over the six month period to September 2008 – i.e. 4.2% in total.

However, there are some risks associated with a fare increase, including the capturing of increased profits by taxi licence holders, and possibly depots/networks, as well as the potential demand response. Ensuring that any revenue increases flow only to taxi operators (who incur LPG costs) would require direct controls over licence assignment fees – a significant intervention. As discussed in section 6.3, such controls are only one approach to addressing the wider issues in relation to income distribution in the industry which the Commission will examine as part of the Review.

The Commission will also give consideration, in the Draft and Final reports, to the benefits of a maximum fare regime in the pre-booked market, to enable taxi operators to mitigate their risks associated with the potential demand response by discounting fares if this is found to be necessary or advantageous.

The undesirable effects of high licence values and assignment fees on the ability of the industry to compete and provide high service standards needs to be addressed, and to this end the Commission intends to give consideration to the effectiveness of the current licence release program in its Draft and Final Reports.

6.1.1 Fare component Variations

Stakeholders have raised a range of issues in relation to fare structures. The Commission will give consideration to the fare structure in the Draft and Final reports of this Review. Given this, and the Commission's preference for the implications of cost pressures in the taxi industry to be given further consideration in the Review, the issue of fare component variations has not been addressed in this Interim Report. As some of the "fixed" elements of the fare structure may recover some of the on-road costs of cabs, it should not be assumed that only the per-kilometre charge would be relevant to an interim price adjustment.

The Commission's preference is for the alternative options to be given further consideration in the Review. If there is an interim price increase, then the Commission's preference is that, prior to its findings on fare structure in the Draft and Final reports of this Review, any fare increase should be applied proportionately to all charges on the metered fare.

However, should this recommendation not be accepted, Table 6.1 provides a breakdown of the current typical taxi fare to assist in formulating other options. Several alternative options for effecting a 4.2% increase are also shown in Table 6.1, including: a 6.2% increase in the distance charge alone; a 24.7% (i.e. 77 cent) increase in the flagfall charge alone; a 20.4% increase in both the flagfall and booking charges; or a 50% increase in the booking charge and a 3.6% increase in the distance charge, are among the options.

Table 6.1 **Fare adjustment options**

	Current fare components	*Factor*[a]	*Revenue per fare component per trip* *Current fare*	*Increase all charges by 4.2%'*	*Increase in distance charge only by 6.2%*	*Increase in flagfall only by 24.7%*	*Proportionate increase in flagfall & booking fee by 20.4%*	*Increase in booking fee by 50% and distance charge by 3.6%*
Flagfall	3.10		3.10	3.23	3.10	3.86	3.73	3.10
Distance charge	1.47	8.4 km	12.35	12.87	13.11	12.35	12.35	12.79
Booking fee	1.30	50% of trips	0.65	0.68	0.65	0.65	0.78	0.98
Waiting time charge	31.5	3.0 min	1.58	1.64	1.58	1.58	1.58	1.58
Late Night Surcharge	20%	15% of trips	0.53	0.55	0.53	0.53	0.53	0.53
Total			18.20	18.97	18.97	18.97	18.97	18.97

[a] Sources: PwC 2007 survey, VTA

6.2 Preliminary views on fare adjustment formulas

In relation to the formula for resetting prices for the next three to five years, the Commission will provide its substantive recommendations in its Final Report, but its preliminary views are presented here.

In relation to the methodology for automated fare adjustments for the next three to five years, three alternative approaches were outlined in the Issues Paper. These included industry-specific cost indices; broad economic cost indices (such as the CPI, the Transport component of the CPI or the Wage Price Index); or a composite cost index approach (combining several indices to more closely reflect input prices).

The relevant objective is to generate a price path equivalent to the outcome in an effectively competitive market. In these circumstances prices will track industry unit costs, including a normal rate of return on capital. The industry unit costs will follow a path equal to movements in the index of input prices, less the total factor productivity improvements achieved.

The Issues Paper also indicated that relevant criteria for evaluating the alternative approaches for automated annual fare adjustments include:

- providing certainty for the taxi industry and for users
- simplicity, with minimum administrative cost
- ensuring cost reflectivity and ongoing viability of the taxi industry, and
- providing strong incentives for efficiency improvement.

While the price path formula is not the main focus of this Interim Report, it is useful to comment on some of the Commission's preliminary views, as this is relevant to the wider question about how future LPG price movements should be dealt with under the price regulation framework.

6.2.1 The three options

Whilst an industry-based cost index is favoured by some Australian jurisdictions as it encompasses costs specific to the taxi industry, this approach is relatively costly and time consuming. For example, IPART reviews NSW taxi fares annually, and Queensland Transport has at times varied fares on a six month basis (or annually if the six month change would not be material). In contrast, a broader economic cost index or a composite cost index approach are simpler to implement, and less costly as they utilise widely published ABS economic cost indices for changes to fares within a pricing period. They also have the potential to provide stronger efficiency incentives.

The Commission's preliminary view is that a detailed examination of industry costs is appropriate at the commencement of each new pricing period (i.e. every three to five years). In the current review the Commission has conducted a broad based survey of taxi operators and drivers for this purpose. This is consistent with VTA's statement that:

Regular estimates of taxi specific costs and productivity trends in the taxi industry based on large random samples are needed if the CPI-X approach is to be used effectively.[31]

However, while the Commission sees merit in such studies at the commencement of each pricing period, it's preliminary view is that it does not support the use of such detailed cost studies during the pricing period. This would be inconsistent with the objective, stated in the terms of reference, of providing for automated fare adjustments within the regulatory period. Furthermore, as the Commission emphasised in the 2005 Taxi Fare Review, resetting prices based on realised cost outcomes would result in a lack of incentives for taxi operators to improve cost efficiency and productivity. It would increase administrative costs if such analysis were carried out frequently.

The Commission has also noted that submissions from the VTA and two taxi drivers indicated dissatisfaction with the current CPI-X approach, as not being sufficiently cost-reflective.

6.2.2 Preliminary preferred fare adjustment formula

The Commission sees merit in the use of a specifically constructed index of input prices which uses a small number of published price indices which are relevant to Victorian taxi industry costs, and weights these by the shares of the respective inputs in industry costs to derive a "composite index of input prices". This approach is used in several Australian jurisdictions.

Price indices that are expected to be relevant for constructing the composite input price index include: the ABS Wage Price Index (**WPI**) for the Transport Industry (for driver costs); the Private Motoring Index (**PMI**) in the CPI, Melbourne (for a number of vehicle-related costs), LPG price indices published by FuelTrac; the Insurance Index in the CPI, Melbourne; and the CPI – All Groups, Melbourne (e.g. for overhead costs).

The Commission would not propose to include license assignment costs in the construction of this index, for reasons already discussed (in terms of its nature as an economic rent) and to avoid the circularity that the inclusion of these fees would introduce into the index.

The composite input price index would normally need to be adjusted for forecast productivity improvements to derive a unit cost path relevant for price setting.

The Commission's preliminary view is that the composite index approach has advantages. It is relatively simple to implement, as it primarily utilises indices published by the Australian Bureau of Statistics (**ABS**), and published LPG price indices. This approach would be designed to generate a price path that adequately tracks costs, which is consistent with ensuring that price levels remain adequate for the industry over the pricing period, while also ensuring that they are not excessive. The composite cost index approach would also provide strong efficiency

[31] VTA submission p.10

incentives. The Commission also expects that a productivity adjustment, in the form of an X-factor, would remain appropriate.

The composite price index approach is consistent with current practice in several other jurisdictions such as the ACT, where it has been effective. It also has a significantly greater degree of support in the taxi industry than the current CPI-X formula. For example, the VTA stated:

> *The composite index based on the Transportation sub-indices of the CPI are a better approach and the use of an industry-specific composite wage-price index is better still from the viewpoint of comprehensively accounting for distinctive cost impacts.*[32]

The use of a weighted index was also supported by taxi driver Mr Wally Hunt[33], and it would be compatible with views expressed in other submissions, for example VCOSS:

> *Increases in the price of fuel and other input costs in recent years may well have increased the operating costs of taxis at a rate greater than the Consumer Price Index (CPI). In the interests of a sustainable industry, mechanisms for recuperating these increased costs are important.*[34]

A notable feature of the composite index approach is that because more than half the weighting is given to the WPI index – which tends to increase at a faster rate than CPI – it will tend to generate higher taxi fare increases over time than a CPI-X approach.

The timing of fare adjustments is a matter the Commission must make recommendations on in its Draft and Final reports.

Preliminary conclusions:

The Commission sees merit in the use of a specifically constructed composite index of input prices, using a small number of published price indices relevant to Victorian taxi industry costs, including LPG price indices. Each index would be appropriately weighted to reflect relative importance of the inputs in total costs. The Commission's preliminary view is that a productivity adjustment would remain appropriate. Such a composite index will also require period re-weighting every 3-5 years to remain a reasonable accurate reflection of the taxi industry cost mix.

6.2.3 VTA's proposed Fuel Price Levy

VTA has proposed:

[32] VTA submission, p.10

[33] Mr Wally Hunt submission, p.4

[34] VCOSS submission, p.3

> *… consideration of the use of a FUEL PRICE LEVY that works in the same way that the levy works in the airline industry. In addition to the yearly changes in prices every 3 months, the government and the taxi industry would announce what the LPG price levy for taxi fares would be. If at any time in the future the price of LPG was to fall the levy would be removed.*[35]

Such an LPG price-related levy would have the benefit of providing an ongoing means of alleviating future fuel price movements. The proposed quarterly price adjustments would better align fares with movements in costs than less frequent adjustments.

At this stage, the Commission believes that this may not be the best of the available options for the longer term, because:

- It would not be consistent with having a predetermined formula and process that provides certainty for the taxi industry and for users, which was previously recommended by the Commission and endorsed by the government. This approach was intended to move away from historical practices, which relied on *ad hoc* price adjustments, with excessive weight given to movements in LPG prices.
- It is not used in any other Australian taxi jurisdiction.
- The significant degree of month-to-month volatility in LPG prices is likely to lead to considerable administrative cost, and taxi fare volatility, associated with quarterly determination of an LPG price levy. It will also impose costs on taxi cab operators.
- There are already a range of add-ons to taxi fares (e.g. credit card charges, airport fees, tolls etc) and a further add-on may not be viewed by customers. It would increase the complexity of fares for taxi users. Consumer representatives have expressed concerns at the lack of transparency to users of fares, and the use of various “add on” charges. An LPG price levy would create greater complexity to users, and may discourage taxi use. A relevant view is expressed by VCOSS:

> *From a community sector perspective, a taxi fare price setting model which is predictable and incremental is preferable.*[36]

However, it may be an appropriate short term measure to alleviate immediate financial pressures on taxi operators associated with increased LPG prices.

Recommendation:

The Commission considers that the VTA’s proposed Fuel Price Levy approach is not the best of the available options for the longer term, but may be an appropriate short-term measure to alleviate immediate financial pressures on taxi operators.

[35] VTA submission, p.7

[36] VCOSS submission, p.3

6.3 Broader Considerations

Preliminary considerations in relation to operator and driver remuneration

As discussed earlier, cost pressures on operators have not emerged exclusively from increased LPG prices since the last fare increase in September 2007. Licence assignment fees have also been an important source of additional costs, and this affects the distribution of income throughout the industry as well. One question is whether the revenue from a fare increase can be directed to specific parties that incur additional costs such as operators incurring the cost of LPG. The Commission has also been asked as part of the current taxi fare review to investigate ways to improve driver remuneration. While this aspect of the terms of reference will be addressed substantively in the Final Report, it is expedient for the Commission to discuss some of the issues in this Interim Report.

Several stakeholders have expressed concerns about current levels of driver remuneration, including VCOSS and taxi driver Mr Hunt. The Commission has previously estimated drivers to be earning on average approximately $7.50 to $8.00 an hour, and many working 12-hour shifts. On the other hand, the submission from taxi driver Mr Griffiths indicates that he estimates his income to be “$13 an hour not including GST but before business expenses” but suggests that as an experienced driver, his income is likely to be higher than most.

The burden on the industry imposed by the returns to licence owners was a significant concern to both of the taxi driver submitters. The capture of profits by licence holders, and perhaps by depots as well, has a direct effect on the earnings of drivers and operators. Without other reforms, a simple fare increase is likely to exacerbate the income distribution issues. Thus it is useful to outline some issues and options relevant to addressing problems with current income distribution and how the regulatory framework affects these.

Operators are central to the Victorian taxi industry. They routinely form relationships with drivers through bailment agreements. They are required by regulation to affiliate with an accredited depot. Many operators do not hold a licence, and thus must lease one on assignment from a licence holder. Any reallocation of income from one party to another must proceed through an operator. However, as not all parties have equal bargaining power, imperfect outcomes can be observed. Licence holders accrue rents from the scarcity of licences, as there are more willing operators than taxi plates available. Industry concentration may contribute to higher network fees, with operators facing limited choices for affiliation. Yet there is also evidence that bailee drivers are poorly remunerated under standardised terms of bailment used throughout the industry.

Asymmetries in information and market power suggest that one option for ensuring that a greater share of revenues accrue to taxi operators or to drivers could be greater regulatory intervention in relation to assignment fees or bailment agreements. This approach is not without precedent. The Western Australian government decided in 1998 to implement a maximum plate lease fee[37]. With respect of driver bailment agreements, WA also imposes a maximum pay-in rate which varies dependent on the shift. Thus, for operators, the amount they pay as an assignee is regulated, as is the amount they receive as a bailor.

Nevertheless, increasing the regulatory burden presents its own drawbacks. As the VTA noted in its submission to the Commission's Issues Paper that "Australia is not a planned economy which sets wages by government fiat"[38]. Furthermore, there would be significant practical difficulties (given the lack of reliable industry data) as well as administrative costs. It is unclear that the social benefits would outweigh the costs.

However, the Commission will further examine the available options when developing recommendations for improving driver remuneration in its draft and final reports. One option to be given further consideration by the Commission was put forward by taxi driver Mr Griffiths:

> *A simple solution is to return to pre Foletta conditions, and require that investors operate a car. They could have this managed by a depot, this would be a simple reform that would simply put the investor return at the end rather than the beginning of the profit cycle.*[39]

An alternative approach to improving income distribution within the taxi industry is to reduce the degree of regulation.

The requirement that operators affiliate with a depot exposes them to costs which may escalate in an environment of imperfect competition. It has already been observed that among depots there is significant market concentration. Market consolidation reduces the degree of competition, thereby reducing the relative bargaining power of taxi operators and drivers. This is further exacerbated by compulsory depot affiliation which mandates that operators deal with a depot irrespective of what conditions are being offered. One driver's submission to the Commission's Issues Paper suggested that:

> *The Commission should consider striking out the requirement for taxis to be affiliated with an "accredited network", and only require taxi owners to be monitored for driver alarms. […] The taxi owners and drivers would then have the freedom to operate under the livery of a "Secondary Network".*[40]

Secondary networks emerged partly in response to customer dissatisfaction with primary taxi networks, and allow drivers to offer their clients direct booking

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[37] The cap currently stands at $355.00 per week – equating to $18,460 per annum. By contrast, annual lease fees in metropolitan Melbourne averaged $25,800 for new assignments negotiated in January.

[38] VTA Submission, p. 15

[39] Mr David Griffiths submission.

[40] Mr Wally Hunt submission, p. 7

services, bypassing the depots. There are currently seven secondary networks[41], which are accredited under the new industry standards introduced at the end of 2007. These secondary networks could bring greater competitive pressures to bear on existing depots, if the compulsory affiliation requirements were relaxed.

The distribution of income within the taxi industry may also be affected by entry restrictions, which can enhance the market power of incumbent licence holders and depots. The Commission will give consideration to whether increasing the degree of competition in the industry would be likely to improve driver remuneration, as well as giving impetus to innovation and service quality. If so, it will identify options to enhance competition.

Relaxing access to licences would reduce the scarcity value of existing licences. For example, this was the case in the ACT, where plate fees dropped by 27% over a 12 months period following the government's announced intention to auction more plates in 2002.[42] The Commission stated in its *Review of Hire Car Licence Fees: Final Report*:

> *The Commission has reviewed the literature on supply restrictions in the taxi and hire car industry. While the Commission recognises that a case can be made on public interest grounds for the use of supply restrictions in the cruising market, it considers that the public interest case for applying such restrictions to the pre-booked segment of the market is far less convincing.*[43]

Greater access to new licenses may also facilitate the retention of experienced drivers in the industry by enabling them to become operators in their own right without being financially exposed to the market power of existing licence holders.

Other options to be examined include a facilitative approach to greater use of non-standardised terms and conditions of bailment. In some jurisdictions there is greater use of the "fixed pay-in" method, under which the driver pays a fixed fee to the operator for use of a cab for a shift, and retains all of the fare revenue and pays for the operation of the cab during that shift. This type of arrangement is used more commonly in Sydney. It has been suggested that it provides drivers with greater efficiency and service quality incentives. On the other hand, initiatives of this kind could not be expected to improve driver incomes in the absence of addressing the fundamental market power balance within the industry.

Preliminary country-specific considerations

In relation to country taxi operations, the Country Taxi Review highlighted that there is a considerable degree of diversity in terms of the competitiveness of taxi services between localities in regional Victoria and for certain types of trips, such as for longer distances. Due to the marginal nature of many taxi operations in smaller towns, there is a relatively delicate balance between the fare levels that will

[41] The Age 2007, 'Underground cabbies put fare service back on the map', 2 December.

[42] ICRC (May 2004) 'Final Report: Determination of taxi fares for the period 1 July 2004 to 30 June 2007', pp 31-32

[43] p.ii

provide sufficient revenue to ensure the continued availability of services, and be affordable for users, and consistent with the ongoing competitiveness of taxi services against alternatives.

Given that many country operators are unable to exert market power even where they might retain a local monopoly, there is limited basis from a consumer interest standpoint for imposing substantial regulation.

One of the options to be examined is whether to remove fare and entry regulation of taxi services in relatively smaller towns. In New Zealand, policymakers have adopted a system of ‘posted prices’ rather than having tariff schedules determined by the regulator. In that country, taxi firms are able to set their own prices which they are required to display prominently both inside and outside their vehicles. There is merit in considering this approach in Victoria, particularly with regard to country taxi operators in smaller towns. A uniform fare schedule across different country zones is unlikely to be able to take into account localised cost pressures and demand differences, whereas a more flexible approach which allows individual operators to better preserve the viability of their businesses may be beneficial.

In the 2005 Taxi Fare Review the Commission highlighted examples of the constraints on competitiveness of some types of services imposed by the existing mandatory fare regime. Therefore, another option to be considered as part of the review is whether allowing taxi operators to discount from their fares where it is advantageous to do so, would be of benefit. At present this form of discounting is only available for contract or regular bookings, or journeys of more than 80km (in country areas).

The competition provided by community transport schemes has an impact on the contract work undertaken by country taxis. The Commission anticipates examining the competitive pressures facing regional Victorian taxi operators, and opportunities for cab operators to negotiate rates for contracted services, in more detail for its Draft and Final Reports. As the Country Taxi Review argued:

> *The Working Group believes that benefits of a more flexible fare structure will be to enable taxi operators to offer more innovative transport solutions to organisations/groups rather than individuals.*[44]

Given the different pressures facing country taxi operators from their metropolitan counterparts, there may be benefit in providing greater capacity for fare and operating flexibility.

6.4 Summary of Conclusions

The Commission’s analysis suggests that there are a number of factors impacting taxi operator returns in addition to LPG prices, not least of which is the cost of renting a taxi licence. Licence values and assignment costs have increased rapidly in recent years, and in light of these trends, further attention needs to be given to

[44] Victorian Country Taxi Review Working Group (2006), op cit, p. 33.

options to address this source of cost pressure. Some options have been suggested by submitters, such as changing the current licence marketing arrangements, and these and other options deserve examination in the Draft and Final Reports of this Review. The sources of increased licence assignment costs and the options to reduce them need to be given careful consideration.

More broadly, the regulatory framework appears to impose some restrictions which may impede the ability of taxi operators to achieve revenue growth, or may be detrimental to driver incomes. A number of options are to be examined in the Draft and Final Reports for increasing the flexibility of taxi operators, and to facilitate efficiency.

The Commission has reached the following conclusions in preparing this Interim Report regarding recent increases in LPG prices. It should be stressed that in reaching these conclusions the Commission is currently undertaking a review which is to examine a broader range of considerations, including driver remuneration, affordability and availability of taxi services. There have been a number of submissions made in relation to these matters, which will be considered through a consultative process in the coming months. Hence, the following conclusions should be regarded as recommendations to deal with a specific issue of concern at this point in time, and should not be seen as pre-determining the outcomes of the overall review.

- The impact of recent increases in LPG prices and accreditation costs is approximately 4% of the total revenue required to operate a taxi and earn a margin (net of assignment fees) commensurate with the level adopted in 2005.
- The increase in the price of LPG is borne entirely by taxi operators, who have also faced increasing assignment fees payable to licence holders.
- Increased input costs since the last review of taxi fares are expected to result in increased fares in 2008.
- After setting fares for 2008, the subsequent adjustment of fares over the next 3-5 years should occur through a pre-determined automated price formula linked more closely to taxi input costs.
- The movement in assignment costs is a matter that relates to the distribution of income between licence holders and taxi operators, and should not warrant changes to the fares paid by taxi users.
- The use of the CPI-X formula has resulted in lower margins for operators than expected, since taxi input costs have grown at a faster rate than the CPI.
- An interim fare increase would alleviate the impacts of increased costs on taxi operators, provided that assignment fees are not increased proportionately.
- A separate levy is not preferred as a long term option, although it could be considered as an interim measure if it provides a means to ensure that this additional revenue is retained by taxi operators
- The merits of a ‘catch up’ increase to offset the unforeseen increases in costs since 2005 will be considered by the Commission in preparing its final report in June 2008, and this will take into account any decision made in relation to an interim increase.

APPENDIX A | TERMS OF REFERENCE

Transport Act 1983

Review of Taxi Fares 2007/08

I, Tim Pallas MP, Acting Minister for Public Transport give notice that in accordance with the provisions of section 186 of the **Transport Act 1983**, I have asked the Essential Services Commission to conduct an investigation into Victoria's taxi-cab fares and report on:

i. the impact of further and sustained upward pressure on liquid petroleum gas (LPG) costs on taxi operators;

ii. an appropriate price setting model to provide for automated fare adjustments for the next 3–5 years, including the timing of such adjustments;

iii. the appropriateness of the taxi fare structure within the current market for taxi-cab services in Victoria;

iv. whether a surcharge on taxi fares on New Year's Eve should form a permanent part of the taxi fare structure for non-metropolitan taxi-cabs and, if so, the amount of such surcharge;

v. whether a surcharge on taxi fares should form a permanent part of the taxi fare structure where the hirer pre-books and is supplied a premium service taxi and, if so, the amount of such surcharge;

vi. the distribution of taxi fare revenue and measures that may be considered by Government to improve taxi driver remuneration; and

vii. information reporting by the taxi industry and performance measurement.

In its investigation and report, the Commission is to have regard to the following factors:

a) the cost pressures on the industry regarding the increase in the price of LPG,

b) the recommendations contained in the Commission's Report – 'Taxi Fare Review 2005' and the subsequent application of the CPI–X pricing model to taxi fares in 2006 and proposed to be applied in 2007;

c) the review of the regulatory structure and operations of Victoria's country taxi industry undertaken by the Department of Infrastructure during 2005/06;

d) the relevance and values of the individual components that, when combined in part or in full, make up the total taxi hiring charge – specifically these are the flagfall, time and distance rate, phone booking fee, Late Night Surcharge (metropolitan taxi-cabs only), Late Night Extra (non-metropolitan taxi-cabs), New Year's Eve taxi fare surcharge (non-metropolitan taxi-cabs) and any

Premium Service Surcharge currently applied in accordance with permit conditions issued by the VTD;

e) the impact on Victorian business and the community including the impact of any proposed variations to taxi fares on the availability and affordability of taxi services to consumers; and

f) the impact on taxi industry participants including licence holders, taxi operators, drivers and employees.

The following directions have been given under section 186 (4) of the Act:

- In conducting the investigation the Commission should have regard to the objectives in section 8 of the **Essential Services Commission Act 2001** where relevant.
- Except as otherwise directed by the terms of reference, the Commission is to conduct the investigation in a manner as described in section 187 of the **Transport Act 1983**.
- The Commission is to provide an interim report in respect of (i) above by 31 January 2008 (or as soon as possible thereafter) and submit its final report to the Minister for Public Transport by 30 June 2008.

This notice supersedes the terms of reference [Review of Taxi Fares 2007/08] published in the Victoria Government Gazette on 14 September 2007.

Tim Pallas MP

Acting Minister for Public Transport

APPENDIX B | CALCULATION OF COMPOSITE INPUT PRICE INDEX

An index of input prices, W, has been estimated using a specifically constructed index which weights together the prices of inputs by their shares in industry costs to derive an index of input prices. The aggregation formula for the composite input price index is:

(Equation B.1) $$\Delta W = \sum_k s_k \ln\left(\frac{w_{kt}}{w_{kt-1}}\right)$$

Where Δ refers to the percentage change, s_k is the share of input *k* in taxi operator costs excluding licence assignment fees, and w_k is the price index of input *k*.

The input price deflators used for calculating the composite input price index are:

- For driver incomes, the ABS Labour Cost Index (i.e. Wage Price Index), Transport industry sector.
- For Motor vehicles, repairs and maintenance, tyres and washing the deflator is the Private Motoring Index (PMI) in the CPI, Melbourne.
- For Fuel (LPG), the price of LPG published by FuelTrac (or the website Motormouth for recent data) is used.
- For Insurances, the Insurance Index in the CPI, Melbourne.
- Other inputs, including network fees, office, uniform and other costs, are deflated using the CPI – All Groups, Melbourne.

The cost share weights used for constructing the composite index are based on the 2004 PwC survey, and shown in Table 4.3 earlier. As mentioned, license assignment costs are not treated as an input for the purpose of constructing this index.

Note that to estimate trends in unit costs, an additional allowance needs to be made for productivity.

Table B.1 **Composite Input Price Index (Jun 2005– Dec 2007)**

	WPI-Trans	*CPI-Melb*	*PMI-Melb*	*INS-Melb*	*LPG*	*Composite Input Price Index*
Weights	*61.8%*	*13.3%*	*10.9%*	*4.7%*	*9.3%*	
Jun-2005	100.0	100.0	100.0	100.0	100.0	100.0
Sep-2005	101.3	101.2	104.1	103.1	104.9	102.0
Dec-2005	102.3	101.6	103.3	107.2	123.6	104.4
Mar-2006	103.4	102.5	104.8	107.6	142.2	106.7
Jun-2006	103.8	103.9	108.7	109.2	127.8	106.7
Sep-2006	105.0	104.6	109.0	113.3	126.8	107.6
Dec-2006	106.2	104.5	104.4	109.6	117.5	106.9
Mar-2007	107.2	104.7	105.0	109.1	121.5	108.0
Jun-2007	108.3	105.9	108.2	110.5	125.1	109.5
Sep-2007	109.5	106.8	107.7	113.9	125.4	110.5
Dec-2007	110.8(e)	107.7	107.1	117.2	149.0	113.3

a All indices rebased to June 2005 = 100.0.

Source: PwC (weights), ABS, Fueltrac

The 3.8% estimated impact of LPG prices is calculated by setting the LPG price index to 100 throughput the period June 2005 to December 2007 and recalculating the composite price index using Equation B.1.

APPENDIX C | INDUSTRY SURVEY ANALYSIS

PRICEWATERHOUSECOOPERS

Essential Services Commission

Review of Victorian Taxi Costs

15 February 2008

Disclaimer

This Report has been prepared by PricewaterhouseCoopers (PwC) at the request of the Essential Services Commission in our capacity as advisors in accordance with the Terms of Reference and the Terms and Conditions contained in the Consultant Agreement between the Essential Services Commission (ESC) and PwC.

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Executive Summary

The upcoming 2007/08 Victorian taxi fare review will be the second major taxi fare review carried out by the Essential Services Commission (ESC). As part of the review, the ESC commissioned PricewaterhouseCoopers (PwC) to undertake a survey of taxi drivers and operators in the four licence zones of Victoria, with the objective to develop the cost profile for a median taxi.

Survey of taxi drivers and operators

Separate driver and operator surveys were developed by PwC and the ESC in close consultation with the Victorian Taxi Directorate (VTD). A total of 6,631 surveys were mailed by the VTD to:

- 2,523 taxi operators (100% of registered operators in Victoria); and
- 4,108 drivers (50% of active drivers in Victoria).

The survey was undertaken over the period November 2007 to January 2008, with the majority of responses completed and returned in early to mid-December. 431 completed survey responses were received, 204 from operators and 227 from drivers.

Median taxi cost profile

The cost profile for a median taxi was based on the cost items from the ESC's June 2005 *Taxi Fare Review Final Report – Taxi Fare Review 2005*, as shown in **Table ES.1**.

The median taxi costs were determined by PwC based on the responses to the survey questionnaire. The questionnaire also obtained information on the operational characteristics of a median taxi (drivers per taxi, jobs per year, kilometres per year, etc.), which are documented in our report and form the key assumptions used to derive the costs per taxi in **Table ES.1**.

As shown in **Table ES.1**, the cost items with the largest weighting in the median taxi profile are driver payments and assignment fee/plate lease costs, which together comprise 72% of total costs. Given the large weight of driver payments (54%) – which are variable by nature being dependent on factors such as kilometres and shifts travelled – taxi costs may be seen to be largely variable in nature. Costs that are fixed, or relatively fixed, i.e. insurance and registration, network fees and assignment fees, comprise 26% of total costs.

Table ES.1 – Cost profile of operating a median Victorian taxi in 2007

Cost item	Annual cost ($)	% of total cost
Driver payments	71,411	54%
Lease/vehicle funding payments	6,653	5%
Assignment fee/plate lease costs	23,418	18%
LPG fuel costs	12,314	9%
Network costs	6,739	5%
Repairs, maintenance and cleaning costs	3,311	2%
Tyre costs	1,130	1%
Insurance and registration costs	4,274	3%
Office/miscellaneous costs	2,521	2%
Variable labour/other driver costs	840	1%
Total cost per median taxi	**132,611**	**100%**
Cost per total km	1.14	
Cost per paid km	2.29	
Estimated total revenue	**142,823**	
Margin	**8%**	
Revenue per total km	1.23	
Revenue per paid km	2.46	
Median fare per job	20.63	

Table ES-2 shows the profile of a median taxi in the metropolitan and outer-suburban licence zone, regional licence zone and country licence zone. The cost profile presented in this table is based on the following respondent numbers to the operator survey: 117 metropolitan respondents; 15 outer-suburban respondents; 31 regional respondents; and 39 country respondents.

As the cost profile in **Table ES-2** indicates, driver payments followed by assignment costs are the most significant cost categories across the licence zones. In addition, while the survey results suggest that country taxis have the lowest total costs and cost per km, the revenue is also the lowest. This may be due to the higher kilometres driven by a median country taxi, with a slightly lower proportion of paid kilometres (47% for a country taxi in comparison to 51% for a metropolitan/outer-suburban taxi).

Table ES-2 – Profile of median metro & outer-suburban / regional / country taxis in 2007

Cost item	Median metro & outer-suburban taxi	Median regional taxi	Median country taxi
Driver payments	71,617	76,830	67,080
Lease/vehicle funding payments	6,648	6,652	6,688
Assignment fee/plate lease costs	24,055	15,340	22,412
LPG fuel costs	12,079	12,365	14,144
Network costs	6,247	10,000	9,000
Repairs, maintenance and cleaning costs	3,179	3,645	4,192
Tyre costs	1,078	1,274	1,467
Insurance and registration costs	4,479	3,750	2,916
Office/miscellaneous costs	2,422	1,920	3,600
Variable labour/other driver costs	786	1,275	1,050
Total cost per median taxi	**132,591**	**133,051**	**132,549**
Cost per total km	1.17	1.02	0.99
Cost per paid km	2.32	2.31	2.10
Estimated total revenue	**143,235**	**153,660**	**134,160**
Margin	**8%**	**15%**	**1%**
Revenue per total km	1.27	1.18	1.01
Revenue per paid km	2.50	2.66	2.12
Median fare per job	20.71	19.70	20.48

1 Introduction

Background to the project

The upcoming 2007/08 Victorian taxi fare review will be the second major taxi fare review carried out by the Essential Services Commission (ESC). As part of the review process, the ESC commissioned PricewaterhouseCoopers (PwC) to undertake a survey of taxi drivers and operators in the four licence zones of Victoria, with the objective to develop an information base of cost inputs and outputs to better inform decisions of changes to fare adjustment methodologies.

In 2005 the Commission undertook its first review of Victorian taxi fares, with the *Taxi Fare Review* 2005 report, which put forward recommendations for fare adjustments, submitted to the Minister in June 2005. The upcoming 2007/08 review will be the second major taxi fare review carried out by the Commission. As a result of the first major review:

- the ESC recommended adopting the CPI-X approach for setting taxi fares, which combines a broad economic cost index with a productivity X-factor (is now in place); and
- a further significant outcome from the 2005 review was the ESC's that additional data collection and analysis was required, which highlights the importance of this survey process.

Prior to the current survey being undertaken, the most recent survey of taxi costs and their relative weightings was undertaken by PwC in 2005 (based on 2000 and 2004 data). This involved survey and data gathering from the Victorian Taxi Directorate (VTD), Victorian Taxi Association (VTA), and eight metro, outer-suburban, regional and rural taxi operators.

The survey process undertaken and presented in this report is the result of a broader and more comprehensive survey of the entire population of operators and half the population of active drivers. The operator survey was mailed to 2,523 taxi operators, and the driver survey was mailed to 4,108 drivers in the metropolitan, outer-suburban, regional and country areas. The licence zones as assumed throughout this report are:

- *metro* – Melbourne;
- *outer-suburban* – Frankston and Dandenong;
- *urban* – Geelong, Ballarat and Bendigo; and
- *country* – remainder of regional Victoria.

Structure of this report

The remainder of this report is structured as follows:

- **Chapter 2** outlines the approach undertaken to develop the 2007 taxi cost profile;
- **Chapter 3** presents the results of the study in terms of the cost components of the profile;
- **Chapter 4** summarises the conclusions of the report;
- **Appendix A** shows the taxi driver survey form; and
- **Appendix B** shows the taxi operator survey form.

2 Approach

Introduction to PwC's approach

PwC's approach to the review of Victorian taxi costs includes:

- data collection through a survey of taxi drivers and operators; and
- development of the cost profile for a median taxi.

Data collection approach

The data collection approach was based on a survey of taxi drivers and operators.

All registered taxi operators and a selection of drivers in Victoria were surveyed as part of this study to ensure a representative sample was obtained.

The survey was developed by PwC and the ESC in close consultation with the VTD to ensure that the survey design adequately captures the relevant costs incurred by the industry, and enables issues to be explored that affect the way in which taxi services are delivered.

Separate surveys were developed for drivers and operators as deemed appropriate for each group. For operators that also drive taxis, there was a separate section inserted at the end of the operator survey to capture driving information. A total of 6,631 surveys were distributed to registered taxi drivers and operators in Victoria by the VTD, with the survey mailed to:

- 2,523 taxi operators (100% of registered operators in Victoria); and
- 4,108 drivers who were not also taxi operators (50% of the active drivers in Victoria).[1]

The survey was undertaken over the period November 2007 to January 2008, with the majority of responses completed and returned in early to mid-December. There were 431 completed survey responses received, including 204 from operators and 227 from drivers (a response rate of 8% for operators and 6% for drivers). This sample size provides a confidence interval of +6.58% for operators and +6.41% for drivers at a confidence level of 95%.[2]

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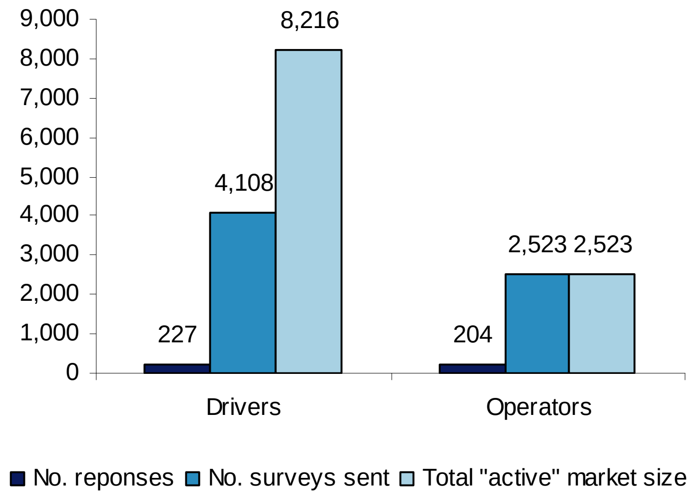
[1] Note: for the purposes of this survey, "active" is defined as a driver that has driven 50 or more times over the last 12 months (every second active driver record was mailed a survey) (Source: 11 February 2008 email communication to PwC from the VTD)

[2] Note: Assuming worst case percentage 50% (Source: http://www.surveysystem.com/sscalc.htm#cineeded)

A brief profile of respondents in terms of the total market size and survey responses is shown in **Figure 1**.

Figure 1 – Profile of respondents by survey type



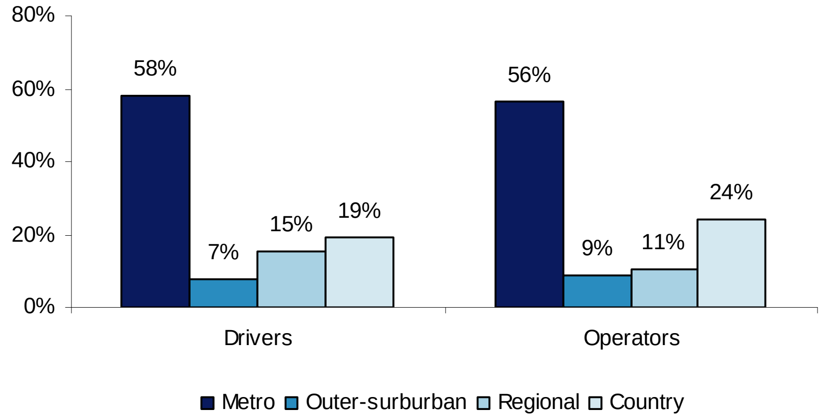
n = 204 operators & 227 drivers

Surveys were received from metropolitan, outer-suburban, regional and country taxi licence zones, with the percentages returned shown in **Figure 2**. Surveys were relatively aligned with the industry as a whole, which is characterised by the following split of licences per licence zone:

- *metro* – 81%;
- *outer-suburban* – 3%;
- *urban* – 5%; and
- *country* – 11%.[3]

[3] Source: 29 January 2008 industry statistics – provided to PwC in 29 January 2008 email communication from the VTD

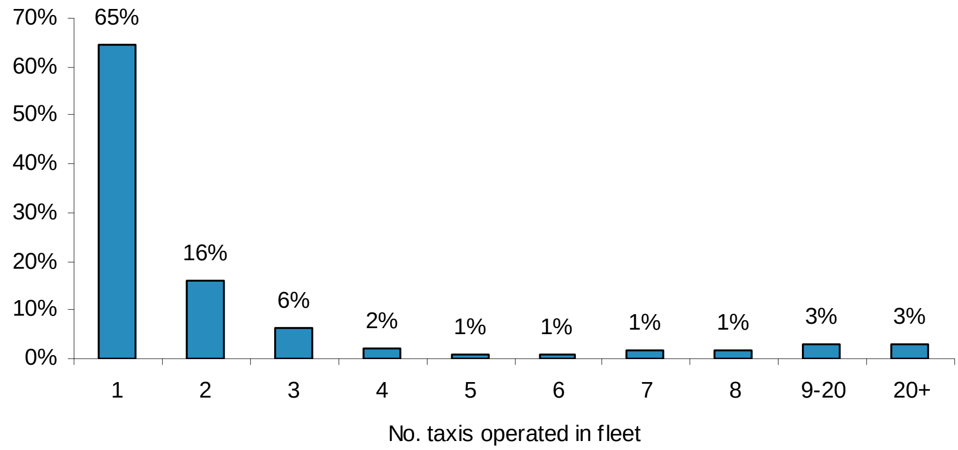
Figure 2 – Profile of respondents by licence zone



n = 202 operators & 227 drivers

Of the operators that responded, the majority (65% per cent) operated only one taxi. The largest number of taxis operated in a fleet by respondents was 60 taxis, with the second highest being 57 followed by 45. The two largest fleets were both operated in the metro area, with the 47-taxi fleet in regional Victoria. A breakdown of the sample by the fleet size is shown in **Figure 3**.

Figure 3 – Profile of respondents by number of taxis operated



n = 201 operators

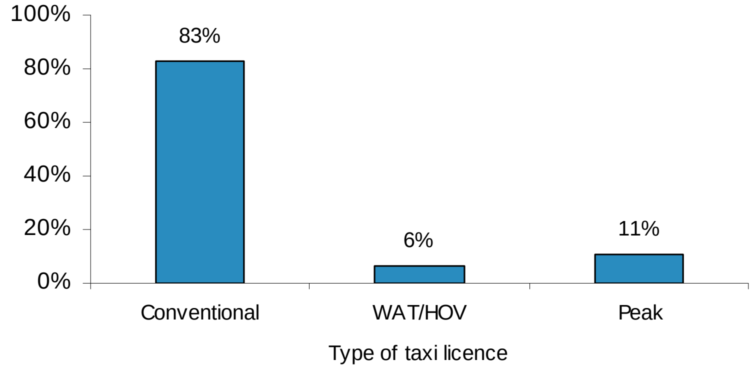
The majority of respondents (83%) operated standard taxis, 6% operated Wheelchair Accessible Taxis (WATs) or High Occupancy Vehicles (HOVs), and 11% operated peak/greentop taxis. Surveys were relatively aligned with the industry as a whole, which is characterised by the following split of licence types:

- *standard taxi licence (includes premium taxis)* – 81%;
- *WAT/HOV licence* – 8%; and

- *peak/greentop licence* –11%.[4]

A breakdown of the survey sample by vehicle type operated is shown in **Figure 4**.

Figure 4 – Profile of respondents by type of licence operated



n = 204 operators

A copy of the taxi driver survey is included in **Appendix A**, and a copy of the taxi operator survey can be found in **Appendix B**.

In the process of analysing survey results, PwC held discussions with a small selection of survey respondents who had indicated their willingness to be contacted relating the survey. In addition, the ESC undertook discussions with industry stakeholders, the VTA and VTD to verify information where possible.

Cost profile development approach

Selection of cost items

In developing the cost profile for a median taxi in Victoria, the cost items were based on those in PwC's May 2005 *Report to the ESC on changes in costs of operating taxis in Victoria 2000 to 2004*, which were also stated in the ESC's June 2005 *Taxi Fare Review Final Report – Taxi Fare Review 2005*.

For individual cost items that comprise less than 2% of total costs, they are included in the components "Office/miscellaneous" or "Variable labour/other driver costs", with the exception of "Tyres", which have remained at 1% of total costs in 2004 and 2007.

As cost items additional to those included in the 2004 cost profile were not found to comprise more than 2% of total costs based on survey results, no

[4] Source: 29 January 2008 industry statistics – provided to PwC in 5 February 2007 email communication from the VTD

new separate cost items have been included in the cost profile. However, the “Office/miscellaneous” and “Variable labour/other driver costs” categories are comprised of costs that vary slightly from the 2004 profile.

Selection of cost values

The cost values proposed for the revised cost profile were based on the survey results, and in certain instances were estimated based on a combination of survey results.

Given the range of costs reported for many cost items, median costs were used for the proposed profile as reported in the driver and operator surveys. Median costs were used to ensure a consistency of approach in the use of survey data, given the potential bias involved in using average costs for items that showed a large spread between highest and lowest cost outcome, and/or included questionable outliers.

Key assumptions behind cost values

This review assesses the median annual cost of operating a taxi in Victoria.

In order to ensure that survey results were based on a median annual taxi’s costs, are set of assumptions were used to convert survey results into an annualised and ‘median’ taxi basis. For example, the survey posed some questions on a weekly or monthly basis, or requested costs on a ‘whole of fleet’ as opposed to ‘per one taxi’ basis, which required adjustment to attain a median taxi profile.

The review makes the following key assumptions:

- each taxi is utilised for 52 weeks a year;
- casual drivers are assumed to generally be used during periods of absence by permanent drivers to ensure that taxis remain operational over this period. Based on this, a Victorian taxi is assumed to have a median number of 1.4 permanent (regular) drivers as derived from the survey;
- the most likely number of taxis operated per operator is 1, which is the median result from the survey;
- all costs are goods and services tax (GST) inclusive;
- all relevant costs incurred in operating and driving a taxi in Victoria have been obtained from the survey of drivers and operators;
- to more accurately reflect a median taxi, survey results have been weighted based on the structure of the actual industry, with results weighted to the split of metropolitan licences (81%), outer-suburban licences (3%), regional licences (5%) and country licences (11%);[5] and

[5] Note: unless referred to specifically as ‘respondent’ results, all results presented in this report are weighted against the licence numbers in the four regions of Victoria.

- annual kilometres (km) travelled (paid and non-paid kilometres) is assumed to be 116,048 km for a median Victorian taxi.[6] This is based on survey results regarding the median number of kilometres travelled in the last shift, analysed alongside the median number of shifts a taxi is operated per week.[7]

A summary of assumptions that have been determined based on median survey results are provided in **Table 1**.

Table 1 – Key assumptions for a median Victorian taxi

Category	Key assumptions for a median Victorian taxi 2007	Medians
Drivers & fleet	Permanent drivers per taxi	1.4
	Taxis per operator fleet	1.0
Shifts & jobs per annum	Shifts per year	472
	Jobs per shift	15
	Jobs per year	6,923
	Length of weekday shift (hrs)	12
	Length of weekend shift (hrs)	11
Kilometres	Total km per year	116,048
	Total km per month	9,671
	% of total km that are paid (I.e. generate fares)	50%
	Total paid km per year	57,967
	Paid km per job	8.4
Whole-of-industry	Total km per year (million)	539.7
	Total paid km per year (million)	269.6
	Total jobs per year (million)	32.2

A summary of assumptions that have been determined based on median survey results for each of the licence zones are provided in **Table 2**.

[6] Note: based on the weighted median of metro, outer-suburban, regional and country licences, which travel medians of 112,320 km, 130,000 km, 130,000 km and 133,380 km respectively based on the survey results.

[7] Note: median kilometres travelled per year influence a number of cost components such as fuel, tyres and maintenance.

Table 2 – Key assumptions for a median Victorian taxi

Category	Key assumptions	Median metro & outer-suburban taxi	Median regional taxi	Median country taxi
Drivers & fleet	Permanent drivers per taxi	1.2	1.50	1.50
	Taxis per operator fleet	0.84	1.00	1.00
Shifts & jobs per annum	Shifts per year	470	520	468
	Jobs per shift	15	15	14
	Jobs per year	6,915	7,800	6,552
	Length of weekday shift (hrs)	12	11	12
	Length of weekend shift (hrs)	11	10	12
Kilometres	Total km per year	112,971	130,000	133,380
	Total km per month	9,414	10,833	11,115
	% of total km that are paid (I.e. generate fares)	51%	44%	47%
	Total paid km per year	57,197	57,720	63,180
	Paid km per job	8.3	7.4	9.6

3 Results

The cost and revenue values obtained for the profile of a median taxi, and our assessment of the appropriate cost for each component, are outlined below.

This chapter presents survey results, states the method used to select cost values, and compares 2007 results with the previous 2004 cost profile. Comparisons with the 2004 profile are undertaken in light of constraints given that the 2004 profile was based on a significantly smaller sample size (based on data from eight metro, outer-suburban, regional and country taxi operators, and VTD and VTA input).

The cost and revenue values in this report are estimated annualised costs/revenues involved in driving and operation of one taxi.

Components of the cost profile

The cost components of that make up the median taxi profile are:

- driver payments;
- vehicle lease/funding payments;
- assignment costs;
- liquefied petroleum gas (LPG);
- network costs;
- repairs, maintenance and cleaning;
- tyres;
- insurance and registration;
- office/miscellaneous; and
- variable labour/other driver costs.

Each of these components is explained below. Some values may appear inconsistent due to rounding.

Driver payments

Survey results indicate that the median annual driver payments per taxi are $71,411, which is indicative of a fare per job of $20.63. This represents 54% of total costs for a Victorian taxi.

The cost estimate for driver payments is calculated based on the results of the operator survey in terms of the median number of permanent drivers per taxi, which is 1.4. This was then combined with the median fare-taking per driver of $50,459 per year to determine the annual driver payment.

The 2007 value for driver payments based on this methodology is not a perfect indicator, as it assumes that casual drivers are used during periods of absence by permanent drivers, with a focus on permanent drivers as the indicator of median drivers per taxi.

Alternative driver payment methodologies:

- an alternative methodology based on the survey responses, which includes casual drivers, is to derive a driver count based on the average number of shifts operated per taxi per week, assuming that a median driver works five shifts per week (i.e. assumes 1.8 drivers per taxi). [8] This results in annual median driver payments of approximately $91,548 or $50,389 per driver (or a fare per job of $26.45); and

- driver payments have been based on the operator survey as opposed to the driver survey because of the estimated underreporting of driver revenue by drivers. Based on driver survey responses relating to total fare take before pay-in and the median fare take (50%), then assuming a median driver works five shifts per week (i.e. 1.8 drivers per taxi), results in annual driver payments of $49,368, or $27,173 per driver. This equates to a fare per job of only $14.26, and does not take into consideration the significant variation in the driver population. For example driver km driven per week range from 250 km to 4,000 km.

In comparison with the 2004 profile, driver payments have increased from 52% to 54% of total costs. The increase in payments from $66,283 in 2004 to $71,411 in 2007 indicate payments are 8% higher than in 2004, and have a compound annual growth rate (CAGR) of 3% from 2004 to 2007. CAGR is a more accurate measure of year-over-year growth than straight percentage growth, as it the rate at which driver payments would have grown if they grew at a steady rate.[9] The growth in driver payments from 2004 indicates the rising cost of labour in Melbourne and Victoria.

Vehicle lease / funding payments

The operator survey results indicate that operators used the following methods to fund their most recent vehicle purchase:

- bank loan (33% of respondents);

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[8] Note: based on median of 11-12 hours per shift and 60 hours per week per median driver.

[9] Note: driver payments are based on a weighted median of licence numbers across the four licence zones.

- hire-purchase (29% of respondents);
- lease (17% of respondents);
- paid cash (19% of respondents); and
- other (2% of respondents) – including insurance claim and chattel mortgage.

Nearly half (49%) of operator survey respondents indicated that the average vehicle age was 1-2 years when purchased, and 43% of respondents indicated that the average vehicle they purchase is new. The remaining 8% indicated that the average vehicle purchased is 3 years old or more. For second hand purchases, the majority are via a dealer as opposed to via a private sale.

Excluding fit outs, the survey results show the median price paid for the most recent vehicle added to the fleet is **$**28,204 (when weighted against the licence numbers in the four zones of Victoria). The survey results also indicate that the median funding term is 5 years with an interest rate of 9%.

Based on the median vehicle value and the median funding terms and rates, annual lease/vehicle finding payments for a median Victorian taxi are $6,653 (5% of total costs in comparison to 4% in 2004). This change may reflect rising interest rates despite an expected decrease in vehicle costs. The 2004 costs did not distinguish vehicle purchases by new and second hand vehicles, and may have allocated a lower weighting to new vehicles than the 2007 survey has indicated.

Assignment / licence plate lease costs

According to the survey results, the median annual assignment cost / cost of leasing a licence plate is $23,418. This cost is in particular impacted by metropolitan costs given that metro licences make up 81% of the industry and have a median cost of $24,000 based on survey responses.

The variation in survey responses to this question was considerable, with responses ranging from $4,224 to $36,000 per annum. This is in part due to the variation in:

- *metro, outer-suburban, regional and country assignment costs* – with median costs of $24,000, $25,500, $15,340 and $22,412 respectively; [10] and
- *conventional, WAT / HOV and peak taxi assignment costs* – with median costs of $25,000, $18,000 and $6,000 respectively.

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[10] Note: the median lease cost of a country licence plate is $22,412 pa based on the survey. This indicates that transferable country licence plate lease costs are nearing metro costs. Transferable country licences (those issued prior to May 2002), make up the majority (95%) of country licences and are those with variable lease costs. In comparison, the remaining 5% of country licences (20 licences) are those leased to operators from the Victorian Government for annual licence fees varying from $1,444 to $4,422 (including licence administration fee), dependent on how many taxis are in the area immediately prior to licence issues. (Source: Victorian Country Taxi Industry Review Working Group 2006, *Country Taxi Review – Final Report*, May 2006, p.40)

The survey results for metropolitan assignment costs are aligned with Bendigo Stock Exchange (BSX) Taxi Market assignment cost data. Metropolitan conventional taxi licence assignments are now able to be traded on the BSX Taxi Market, which commenced in 2006. Over 2007, BSX Market historical data indicates that the average (mean) assignment cost as traded over the year is $24,526.87. The licence assignment costs vary from an average of $24,003.04 pa traded in January 2007, to an average of $25,405.65 pa as traded in November 2007.

In comparison to 2004 assignment costs, the median annual cost to operators has increased from $20,580 to $23,418 in 2007, which indicates a 4% year-over-year CAGR. The proportion of total costs over this time has increased from 16% in 2004 to 18% in 2007.

It should be noted that not all plates are leased by operators, rather some operators buy their own plates and fund them with debt which result in different loan repayments to the lease payments, and other operators own their plates, incurring no costs.

LPG fuel cost

The survey results indicated that 98% of taxi vehicles use LPG fuel, with the remaining 2% using either diesel or unleaded. As a result LPG fuel survey results dominate this cost component. In addition, survey responses indicate that 90% to 96% of operators pay for fuel (from the driver and operator surveys respectively), so the annual median fuel cost has been based on responses from the operator survey.

Combining operator median fuel prices per litre (for the last price paid) with estimates for fuel usage (i.e. the number of litres per 100 km obtained) a cost per kilometre was derived that was weighted against the four licence zones. This was then combined with the annual kilometres travelled for each licence zone to determine an annual cost based on distance travelled.[11]

Survey results relating to fuel usage and costs indicate that the median price paid by drivers per litre of fuel is $0.59 per litre, with a median fuel consumption rate of 6 kilometres per litre obtained (or 17 litres per 100kms). Based on the above assumptions, the annual cost of fuel is $12,314 per annum or 9% of total costs.

The $12,314 annual fuel cost is higher in comparison to the 2004 fuel cost, which was $10,019 or 8% of total costs. The higher 2007 costs are indicative of a 7% year-over-year CAGR from 2004. The variances in 2004 and 2007 fuel costs are in part explained by:

- 2004 fuel cost was based on actual FuelTrac fuel prices as opposed to survey data (which presented higher fuel costs);
- km travelled vary significantly from 11,709 km per month in 2004 to 9,671 km per month in 2007 – which is in part due to a variance in data gathering methodology (with the 2004 survey only including eight operators); and

[11] Note: See Chapter 2, p.11 for method of determining kilometres travelled.

- fuel cost per 100km has increased from $7.13 per 100 km in 2004, to $10.61 per 100 km in 2007. This trend aligns with FuelTrac LPG trends for Melbourne, which indicate 2004 LPG prices ranged from $0.30 to $0.50 per litre, in comparison to 2007 prices that range from $0.50to $0.70 per litre.[12]

Network costs

Victorian taxi operators are required to operate taxis from depots authorised by the Government. Depots are network service providers that provide a centralised booking and dispatch service.[13]

Based on the survey results, median network fees are $6,739 per annum (5% of total costs. Survey results indicate that network costs vary significantly based on the licence zone, with metro costs the lowest with a median of $6,180, and country and regional costs between $9,000 and $10,000 per year. This indicates that metropolitan depots achieve comparative economies of scale given the number of metro taxis.

In comparison to the 2004 network costs, the proportion of total costs has remained unchanged at **5%** of total costs. In terms of annual cost, it has increased from the 2004 level of $5,831 at a year-over-year CAGR of **5%**.

Repairs, maintenance and cleaning

The survey collected information on repairs, maintenance and cleaning costs per vehicle, which are based on the following sub-components:

- *maintenance labour cost* – based on the median cost per hour and the median number of hours spent on maintenance per taxi per month for each of the four licence zones;
- *repairs and maintenance cost* – based on the median cost of a major and minor service for each of the four licence zones, assuming that services are undertaken every 15,000 km, on a rotational basis of two minor services then one major service; and
- *cleaning cost* – based on the median weekly cost for a basic clean.

[12] Source: Australian Automobile Association, *FuelTrac Average monthly capital city LPG prices (cpl)* (Feb 1999 – Feb 2008), http://www.aaa.asn.au/petrol/LPG.pdf

[13] Source: Department of Infrastructure Website 2008, *Structure of the taxi industry*, http://www.doi.vic.gov.au/doi/internet/vehicles.nsf/AllDocs/712BF0EEC0458993CA256F320020A3FB?OpenDocument#depots

Maintenance labour cost

Based on the survey results, operators incur a median of 7 hours of maintenance per month per taxi, at a median cost of $53.30 per hour. This results in an annualised maintenance labour cost per taxi of $373.

Not included in this cost basis is that a significant proportion of operators (10%) indicate they carry out maintenance themselves. These drivers have chosen to absorb these costs rather than pay for them out of earnings.

As with many answers in the survey, there was a large range of responses, with hourly labour costs ranging from $0 to $72 per hours, and the hours spent on maintenance ranging from 2.5 to 41 hours per month.[14]

Repair and maintenance cost

Based on the survey results, 80% of respondents typically purchase manufacturer made parts and panels, and 20% typically purchase generic parts. None of the respondents indicated they use second hand parts and panels. In addition, survey results show that the majority (88%) of respondents conduct regular minor and major services, with 11% undertaking regular minor services only, and 2% undertaking reactive services only.

As with the 2004 cost profile (but differing from the NSW taxi cost index), major repairs are generally covered by insurance costs and not included in this category.

The cost of a median minor service is $158 and the cost of a median major service is $525. Based on these costs and the assumption that services are undertaken every 15,000 km, on a rotational basis of two minor services then one major service, the median annual repair and maintenance cost is $1,868.[15]

Cleaning cost

Based on the survey results, 98% of respondents carry out cleaning on a weekly basis, with the remaining 2% cleaning over longer (e.g. monthly) periods. The survey asked respondents the weekly cost for a basic wash, with the resulting annual median $1,070.[16]

The 2004 cost profile did not provide a breakdown into maintenance labour, repairs and maintenance, and cleaning costs, presenting these as a total of $5,553 per annum (or 4% of total costs). This is significantly higher than the 2007 survey results, which indicates total repair, maintenance and cleaning costs of $3,311 (or 2% of total costs). The difference in 2004 and 2007 outcomes suggests a year-on-year –16% CAGR from 2004. The difference between the two years' data may be explained by the 2004 report indicating

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[14] Note: Country operators reported the highest median maintenance labour costs, with annual costs 16% higher than the median across the industry.

[15] Note: Country operators reported the highest median repair and maintenance costs, with annual costs 34% higher than the median across the industry.

[16] Note: Country operators reported the highest median cleaning costs, with annual costs 17% higher than the median across the industry; which is in part linked with 100% of respondents indicating they undertake cleaning on a weekly basis.

that “most respondents were not very clear about the actual costs” that made up this cost component, which suggests that the 2004 costs were not reliable.

Tyres

Based on survey results, the cost of one median tyre is $117, excluding balance and alignment. The cost per tyre varies dependent on the licence zone, ranging from a median of $73 for outer-suburban taxis, to $120 for metro taxis.

The survey indicated that operators replace tyres every 48,095 km (metro taxis have a higher median km than taxis in other licence zones). Based on tyre replacement occurs at this km level and the median annual km travelled of 116,048 km, and assuming that all four tyres are replaced on each occasion, each set of tyres needs to be replaced between 2.2 to 3.7 times per year (dependent on the licence zone).

These assumptions result in a median annual tyre cost of $1,130, which is 1% of total costs. The 2004 tyre costs, which included a mix of new tyres, remoulds or retreads based on the eight operators surveyed, were lower at $683 per annum, or 1% of total costs. This indicates a year-on-year CAGR of 18% from 2004 to 2007. The difference in costs is likely indicative of a broader sample of operators included in the 2007 survey, which have encompassed 204 operators in contrast to 8 in the 2004 survey.

Insurance and registration

This cost component includes registration, compulsory third party and insurance costs.

Registration and compulsory third party insurance (Transport Accident Commission Charge (TAC)) were provided in the taxi operator survey, with the variance between respondents consistent with VicRoads TAC, which vary dependent on risk level. The median annual registration and TAC costs provided in the survey is $2,056.

For other insurances extending beyond the compulsory insurances, such as comprehensive insurance and third party property, the survey results indicate that a range of different arrangements are in place amongst operators. For example, the median comprehensive insurance cost from the survey is $1,778; however this is based on responses ranging from $180 to $9,000 per annum (with a response rate of 87%). Likewise, the median annual third party property insurance cost from the survey is $440, though this is based on responses ranging from $150 to $3,900 per annum, and a response rate of only 25%.

The issues with variability of data reflect similar issues with comparing 2007 insurance and registration costs with the 2004 cost profile. In 2004 this component was $5,003 and 4% of total costs, in comparison to $4,274 and 3% of total costs from the 2007 survey results (or a decrease in insurance and registration costs of –5% year-over-year CAGR).

Office/miscellaneous costs

The office / miscellaneous cost category includes expenditure on items such as phone, electricity, accountant fees, administrative staff wages, rent, computers, and other related costs.

The survey questionnaire posed a question surrounding these costs, which achieved a response rate of 86%. There was significant variation in the response to this question, with costs ranging from $10 to $25,000 per month.

According to the survey results, the median annual office/miscellaneous cost is $2,521, or 2% of total costs. In comparison, this cost component was $5,247 per annum in 2004, or 4% of total costs. Given that the 2004 costs were based on a survey of eight operators in comparison to 204 operators in the 2007 survey, it is likely that the results are not perfectly comparable.

Variable labour/other drivers' costs

Included in variable labour and drivers costs are workers compensation payments, driver uniforms, and driver entitlements.

The median annual variable labour/other driver cost are $840 or 1% of total costs. This consists of:

- median cost of $275 per annum for drivers uniforms (based on a 94% response rate);
- median cost of $565 per annum for workers compensation, or a median of 1% of driver payments (based on a 77% response rate); and
- median cost of $0 for driver entitlements (sick leave and holiday pay) based on a 93% response rate. (For the 9% of operators that reported paying driver entitlements, their median annual cost is $500 per annum.)

These sub-categories of costs total $840 per annum (1% of total costs), which in comparison to the 2004 annual cost of $3,229 (3% of total costs), indicates a year-on-year CAGR of –36%.

The difference in costs between these years is primarily related to the different sub-categories of costs included. In 2004, additional costs such as income protection insurance, training and superannuation were included in this cost component; however in the 2007 survey these costs were not included as significant costs for operator respondents, and so have not been included in the 2007 cost profile. For sub-categories such as training costs, these are generally incurred by drivers or networks, and not by operators indicating that these costs are included in the cost profile as part of driver payments or network fees.

Median taxi profile

Table 3 presents the cost profile for operating a median Victorian taxi in 2007. This is presented alongside the profile of operating a taxi based on the smaller-scale survey undertaken in 2004.

Table 3 – Profile of a median Victorian taxi in 2007 and 2004

Cost item	2007 profile ($)	2007 % of total costs	2004 profile($)	2004 % of total costs	CAGR from 2004 to 2007 (%)
Driver payments	71,411	54%	66,283	52%	3%
Lease/vehicle funding payments	6,653	5%	5,397	4%	7%
Assignment fee/plate lease costs	23,418	18%	20,580	16%	4%
LPG fuel costs	12,314	9%	10,019	8%	7%
Network costs	6,739	5%	5,831	5%	5%
Repairs, maintenance and cleaning costs	3,311	2%	5,553	4%	-16%
Tyre costs	1,130	1%	683	1%	18%
Insurance and registration costs	4,274	3%	5,003	4%	-5%
Office/miscellaneous costs	2,521	2%	5,247	4%	-22%
Variable labour/other driver costs	840	1%	3,229	3%	-36%
Total cost per median taxi	**132,611**	**100%**	**127,825**	**100%**	**1%**
Cost per total km	1.14	N/A	0.91	N/A	8%
Cost per paid km	2.29	N/A	N/A	N/A	N/A
Estimated total revenue	**142,823**	N/A	**132,566**	N/A	**3%**
Margin	**8%**	N/A	**4%**	N/A	**0%**
Revenue per total km	1.23	N/A	0.94	N/A	9%
Revenue per paid km	2.46	N/A	N/A	N/A	N/A
Median fare per job	20.63	N/A	N/A	N/A	N/A
Total industry revenue (million)	664.27	N/A	N/A	N/A	N/A

The estimated revenue per median taxi in **Table 3** is based on double the driver payments given that survey responses indicate fare take is divided 50% between drivers and operators.

As indicated in **Table 3**, the margin of a median Victorian taxi is approximately 8% based on the 2007 taxi survey. The change from the 2004 margin of 4% is likely related to the 2004 survey covering a sample of only eight operators, which is not as representative as the 2007 sample of 227 drivers and 204 operators. Given that the survey results suggest that total costs and revenues have increased while kilometres travelled have decreased this results in both a higher cost per km and revenue per km.

Table 4 shows the profile of a median taxi in the metropolitan and outer-suburban licence zone, regional licence zone and country licence zone.

Table 4 – Profile of median metro & outer-suburban / regional / country taxis in 2007

Cost Item	Median metro & outer-suburban taxi	Median regional taxi	Median country taxi
Driver payments	71,617	76,830	67,080
Lease/vehicle funding payments	6,648	6,652	6,688
Assignment fee/plate lease costs	24,055	15,340	22,412
LPG fuel costs	12,079	12,365	14,144
Network costs	6,247	10,000	9,000
Repairs, maintenance and cleaning costs	3,179	3,645	4,192
Tyre costs	1,078	1,274	1,467
Insurance and registration costs	4,479	3,750	2,916
Office/miscellaneous costs	2,422	1,920	3,600
Variable labour/other driver costs	786	1,275	1,050
Total cost per median taxi	**132,591**	**133,051**	**132,549**
Cost per total km	1.17	1.02	0.99
Cost per paid km	2.32	2.31	2.10
Estimated total revenue	**143,235**	**153,660**	**134,160**
Margin	**8%**	**15%**	**1%**
Revenue per total km	1.27	1.18	1.01
Revenue per paid km	2.50	2.66	2.12
Median fare per job	20.71	19.70	20.48

As with **Table 3**, the estimated revenue per median taxi in **Table 4** is based on double the driver payments given that survey responses indicate fare take is divided 50% between drivers and operators. The cost profile presented in this table is based on the following respondent numbers to the operator survey: 117 metropolitan respondents; 15 outer-suburban respondents; 31 regional respondents; and 39 country respondents.

As the cost profile in **Table 4** indicates, driver payments followed by assignment costs are the most significant cost categories across the licence zones. In addition, while the survey results suggest that country taxis have the lowest total costs and cost per km, the revenue is also the lowest. This may be due to the higher kilometres driven by a median country taxi, with a slightly lower proportion of paid kilometres (47% for a country taxi in comparison to 51% for a metropolitan/outer-suburban taxi).

4 Conclusions

The cost and revenue profile of a median Victorian taxi is shown in **Table 5**.

Table 5 – Profile of a median Victorian taxi in 2007

Cost/revenue item	Cost/revenue ($)	% of total cost
Driver payments	71,411	54%
Lease/vehicle funding payments	6,653	5%
Assignment fee/plate lease costs	23,418	18%
LPG fuel costs	12,314	9%
Network costs	6,739	5%
Repairs, maintenance and cleaning costs	3,311	2%
Tyre costs	1,130	1%
Insurance and registration costs	4,274	3%
Office/miscellaneous costs	2,521	2%
Variable labour/other driver costs	840	1%
Total cost per median taxi	**132,611**	**100%**
Cost per total km	1.14	
Cost per paid km	2.29	
Estimated total revenue	**142,823**	
Margin	**8%**	
Revenue per total km	1.23	
Revenue per paid km	2.46	
Median fare per job	20.63	
Total industry revenue (million)	664.27	

As shown in **Table 5**, the cost items with the largest weighting in the median taxi profile are driver payments and assignment fee/plate lease costs, which together comprise 72% of total costs. Given the large weight of driver payments (54%) – which are variable by nature being dependent on factors such as kilometres and shifts travelled – taxi costs may be seen to be largely variable in nature. Costs that are fixed, or relatively fixed, i.e. insurance and registration, network fees and assignment fees, comprise 26% of total costs.

Appendix A

Taxi Driver Survey

Dear Taxi Driver,

You are invited to participate in a survey on taxi costs which will be used by the Essential Services Commission (ESC) in their review of taxi fares. The ESC has been requested by the Minster for Public Transport to conduct a review of taxi fares for 2007/08 and this survey will assist the ESC in carrying out this role.

Survey responses need to be lodged with PricewaterhouseCoopers (PwC) no later than 20 December 2007.

Managing the Survey

PwC has been engaged to manage the survey and report on the results to the ESC.

Survey Participation

A sample of all taxi drivers have been invited to participate in this survey. A related survey has been sent to taxi operators.

You are strongly encouraged to participate as this will help the ESC obtain a better understanding of the costs associated with operating and driving a taxi. Please answer each question carefully.

Privacy

This survey will not be released to any third parties and survey responses will be destroyed following processing. All surveys will be treated as confidential.

The survey contains an optional cell to provide your name and contact details. Whilst providing your contact details is not mandatory, we encourage you to provide a daytime contact number in the event that PwC needs to clarify aspects of your survey response.

How Do I Return My Survey?

Your survey responses can be delivered in 2 ways:

1. Fax the completed form to: (02) 8286 1734
2. Fill-in the hardcopy attached to this letter and return in the pre-paid envelope provided.

If you have any questions in relation to this survey feel free to contact Sarah Latham at PwC on (02) 8266 1734

Yours sincerely,

Michael Cunningham
Manager Industry Sectors & Special References
Essential Services Commission

Taxi Driver Survey

☐ Please tick most appropriate answer **ALL COSTS SHOULD INCLUDE GST**
Should you need help completing this survey, please call Sarah Latham at PricewaterhouseCoopers on (02) 8266 1734.

Surname (optional): **First name (optional):**	
Contact ph number (optional): **Name of Network:** **Residential postcode:**	
Are you happy to be contacted to discuss this survey? Yes ☐ No ☐	
1) Place where you usually drive	Metro (Melbourne) ☐ Outer Suburban (Frankston Dandenong) ☐ Urban (Geelong, Ballarat, Bendigo) ☐ Country (remainder of regional Victoria) ☐
2) Type of taxi driven	Standard sedan or station wagon ☐ Wheelchair Accessible Taxi (WAT) ☐ Premium Silver service ☐ Peak / Green top ☐ High Occupancy Vehicle (HOV) / Maxi ☐ (includes taxi with capacity for 2 wheelchairs)
3) Average number of km you drive in your taxi per week	less than 499 ☐ 500-749 ☐ 750-999 ☐ 1,000-1,249 ☐ 1,250-1,499 ☐ 1,500-1999 ☐ 2,000-2,999 ☐ 3,000-4,000 ☐ more than 4,000 ☐
4) Which shifts do you generally drive each week?	Mon AM ☐ Tues AM ☐ Wed AM ☐ Thurs AM ☐ Fri AM ☐ Sat AM ☐ Sun AM ☐ Mon PM ☐ Tues PM ☐ Wed PM ☐ Thurs PM ☐ Fri PM ☐ Sat PM ☐ Sun PM ☐
5) Average hours worked per shift (Friday & Saturday)	Less than 5 hours ☐ 6 hours ☐ 7 hours ☐ 8-hours ☐ 9 hours ☐ 10 hours ☐ 11 hours ☐ 12 hours ☐ 13 hours ☐ 14 hours ☐ 15 hours ☐ More than 15 hours ☐
6) Average hours worked per shift (Sunday-Thursday)	Less than 5 hours ☐ 6 hours ☐ 7 hours ☐ 8-hours ☐ 9 hours ☐ 10 hours ☐ 11 hours ☐ 12 hours ☐ 13 hours ☐ 14 hours ☐ 15 hours ☐ More than 15 hours ☐
7) What is the average revenue for the following types of shifts?	**Shift** — **Average Revenue** *Weekday (Mon-Fri)* — Revenue per shift $__________ *Week night (Mon-Thurs)* — Revenue per shift $__________ *Weekend day (Sat-Sun)* — Revenue per shift $__________ *Friday night* — Revenue per shift $__________ *Saturday night* — Revenue per shift $__________ *Sunday night* — Revenue per shift $__________
8) What is the basis of your driver engagement?	a) Full-time Bailee ☐ If Full-time Bailee, how many weeks did you work last year? ________weeks b) Casual Bailee ☐
9) What is the payment arrangement you operate under?	**a) Percentage of fare revenue (e.g. 50/50 split)** ☐ If so, what percentage of fare revenue do you get? ____% **OR** **b) Fixed pay-in** ☐ If so, how much is the pay-in? $______ per shift
10) When you entered into your driver engagement were you offered a choice between different payment	Yes ☐ No ☐

arrangements (see Question 9)?	
11) What is your total fare take before pay-in?	$_________ per week **(not including tolls)** **How much on average is collected in tolls?** $___________ per week **How many incidents of fare evasion have you encountered in the previous year?** ________ incidents
12) Do you receive entitlements, such as sick leave or holiday pay?	No ☐ Yes ☐ If yes, how much do you receive? $__________ per year **OR** _________ days per year
13) What costs do you cover out of your share of revenue?	**Daily wash and vacuum** ☐ If so, what is the cost? $____ per week **Mobile phone costs (calls and/or SMS for contacting passengers upon approach)** ☐ If so, what is the cost per week? $____ per week **Cleaning / other maintenance on your driver uniform** ☐ If so, what is the cost per week? $____ per week **GPS navigation device** ☐ If so, what is the cost? $____ **Administration and paperwork costs** (e.g. worksheets and pay-ins) ☐ If so, what is the cost? $____ per week **OR** _________ hours per week How often is this cost incurred?_______ **Other** ☐ If so, Please specify ______________________at $______every_________ _______(time period) ______________________at $______every_________ _______(time period) ______________________at $______every_________ _______(time period)
14) Fuel use and cost	Fuel type: LPG ☐ Diesel ☐ Unleaded ☐ Last price paid $______/litre _____km per litre obtained
15) Who usually pays the fuel costs?	You (i.e. after the end of shift settlement) ☐ The Operator ☐
16) About your last shift **If possible this information should be obtained from the meter** **Please provide a copy of the meter printout if the meter has that facility**	**Date:___________ Time: from________ am/pm to __________am/pm** **Number of passenger trips provided: ________________(number)** **Number of radio bookings accepted (if information available): ____________(number)** **Number of kilometres travelled:__________________(kms)** **Number of booked kms:___________(kms)** **Number of kilometres travelled for which fares were generated: _________(kms) OR _________% of km** **Estimated waiting time: ___________(hours per shift)** **Odometer reading at beginning of last shift __________(kms)** **Odometer reading at end of last shift __________(kms)**
16) Use of toll roads (as compared to alternative routes)	**Frequency of use:** Never ☐ Rarely ☐ Regularly ☐ Always ☐ **Percentage time saving per trip:** Less than 10% ☐ 11-20% ☐ 21-30% ☐ more than 30% ☐ **Do you usually use toll roads without passengers on the return trip?** Yes ☐ No ☐
17) Change in proportion of fare generating kilometres, compared to this time last year	☐ **No change, the same proportion of fare generating kilometres as last year** ☐ **There has been an increase in fare generating kilometres** ☐ **There has been a decrease in fare generating kilometres**

18) Rank the following in terms of the frequency of the trips you make on average? **(from 1–most frequent, to 6-least frequent)**	2 kms or less _________ >2 – 5 kms _________ >5 -10 kms _________ >10 -15 kms _________ >15 -20 kms _________ Greater than 20kms _________

Appendix B

Taxi Operator Survey

Dear Taxi Operator,

You are invited to participate in a survey on taxi costs which will be used by the Essential Services Commission (ESC) in their review of taxi fares. The ESC has been requested by the Minster for Public Transport to conduct a review of taxi fares for 2007/08 and this survey will assist the ESC in carrying out this role.

Survey responses need to be lodged with PricewaterhouseCoopers (PwC) no later than 20 December 2007.

Managing the Survey

PwC has been engaged to manage the survey and report on the results to the ESC.

Survey Participation

All taxi operators have been invited to participate in this survey. A related survey has been sent to a sample of drivers.

You are strongly encouraged to participate as this will help the ESC obtain a better understanding of the costs associated with operating and driving a taxi. Please answer each question carefully.

Privacy

This survey will not be released to any third parties and survey responses will be destroyed following processing. All surveys will be treated as confidential.

The survey contains an optional cell to provide your name and contact details. Whilst providing your contact details is not mandatory, we encourage you to provide a daytime contact number in the event that PwC needs to clarify aspects of your survey response.

How Do I Return My Survey?

Your survey responses can be delivered in 2 ways:

2. Fax the completed form to: (02) 8286 1734
2. Fill-in the hardcopy attached to this letter and return in the pre-paid envelope provided.

If you have any questions in relation to this survey feel free to contact Sarah Latham at PwC on (02) 8266 1734

Yours sincerely,

Michael Cunningham
Manager Industry Sectors & Special References
Essential Services Commission

Taxi Operator Survey

☐ Please tick most appropriate answer. **ALL COSTS SHOULD INCLUDE GST.**
Should you need any help completing this survey, please call Sarah Latham at PricewaterhouseCoopers on (02) 8266 1734

Surname (optional):	**First name (optional):**			
Contact phone number(optional):	**Name of Network:**	**Residential postcode:**		
Are you happy to be contacted to discuss this survey?	Yes ☐ No ☐			

1) Place where you usually drive	Metro (Melbourne) ☐ Outer Suburban (Frankston Dandenong) ☐ Urban (Geelong, Ballarat, Bendigo) ☐ Country (remainder of regional Victoria) ☐				
2) Number and type of taxis operated	Standard sedan or station wagon ☐ Number operated ______ Wheelchair Accessible Taxi (WAT) ☐ Number operated ______ Premium / Silver service ☐ Number operated ______ Peak / Green top ☐ Number operated ______ High Occupancy Vehicle (HOV) / Maxi taxi ☐ Number operated ______ (includes taxi with capacity for 2 wheelchairs)				
3) Number of types of taxi licence	Conventional ___ ------	WAT/HOV ___ --------	Peak Service ___ ---	Other ___------------	
4) Status	Driver only ☐	Operator only ☐	Operator & Driver ☐	Operator, Driver & licensee ☐	Owner only ☐
5) Number of drivers by engagement basis	Casual Bailee ☐ _______ number of drivers Permanent Bailee ☐ _______ number of drivers Driven by owner/operator ☐				
6) If leasing licence (plate), what is the cost per year?	$_____,000 **If plate funded by debt: Funding term** __ years **Interest rate_____**% **Residual_____**% **Deposit paid** $**_____**,000				
7) What is the estimated value of your licence(plate) type (if owned)?	$**_______**,000				
8) Average vehicle age when purchased	New ☐ 1 year ☐ 2 years ☐ 3 years ☐ 4 years ☐ More than 5 years ☐				
9) Typical approach to purchase	New via dealer ☐ 2nd hand via dealer ☐ 2nd hand via private sale ☐ 2nd hand at auction ☐				
10) Price paid for most recent addition to the fleet (on-road including GST) <u>EXCLUDING</u> taxi fit-out costs (e.g. meter, camera, LPG conversion, accessibility conversion costs)	$**____**,000 Paid _____ years ago Vehicle type: ____ **OR** If you bought your vehicle with fit-outs included, what was the price paid? $**____**,000 Paid _____ years ago				

	Vehicle type: ____
11) Most recent purchase funding method	Paid cash ☐ Lease ☐ Hire purchase ☐ Bank loan ☐ Other ☐ (Please specify) _________________
12) Funding details (if relevant)	**Funding term** ____ years **Interest rate** _____% **Residual** _____% **Deposit paid** $____,000
13) Average kilometres of travel per taxi per week	less than 1,000 ☐ 1,000-1,499 ☐ 1,500-1,999 ☐ 2,000-2,499 ☐ 2,500-2,999 ☐ 3,000 – 4,000 ☐ more than 4,000 ☐
14) Average number of day & night shifts operated per taxi per week	0-6 ☐ 7 ☐ 8 ☐ 9 ☐ 10 ☐ 11 ☐ 12 ☐ 13 ☐ 14 ☐
15) Average hours worked per taxi per shift (Friday & Saturday)	Less than 5 hours ☐ 6 hours ☐ 7 hours ☐ 8-hours ☐ 9 hours ☐ 10 hours ☐ 11 hours ☐ 12 hours ☐ 13 hours ☐ 14 hours ☐ 15 hours ☐ More than 15 hours ☐
16) Average hours worked per taxi per shift (Sunday-Thursday)	Less than 5 hours ☐ 6 hours ☐ 7 hours ☐ 8-hours ☐ 9 hours ☐ 10 hours ☐ 11 hours ☐ 12 hours ☐ 13 hours ☐ 14 hours ☐ 15 hours ☐ More than 15 hours ☐
17) Maintenance provider	Self maintenance ☐ Taxi base garage ☐ Mainly small garage ☐ Mainly Franchise (e.g. Ultratune) ☐ Dealer workshop (e.g. Ford dealer) ☐ Other ☐ (Please specify) ______
18) Maintenance strategy	Regular minor services only ☐ Regular minor & major services ☐ Reactive (only to fix a breakdown) ☐
19) Maintenance labour cost (if known)	**Cost per hour** Just my time☐ less than$30☐ $30-$34☐ $35-$39 ☐ $40-$44☐ $45-$49☐ $50-$54☐ $55-$59☐ $60-$64☐ $65-$69☐ $70+☐ **Average number of hours spent on maintenance per taxi per month** Less than 5 ☐ 5-9 ☐ 10-15 ☐ 16-20 ☐ 21-24 ☐ 25-30 ☐ 31–35 ☐ 36-40 ☐ More than 41 ☐
20) Typical type of parts and panels	Manufacturer made (e.g. Ford) ☐ Generic parts (e.g. Repco) ☐ 2nd hand parts☐
22) Total cost of last minor service	$__________
23) Total cost of last major service	$__________
24) Average kms per tyre replacement	30,000km ☐ 35,000km ☐ 40,000km ☐ 45,000km ☐ 50,000km ☐ More than 50,000km ☐
25) Cost per tyre	$__________ (excl balance/alignment)
26) Average operator time per week spent on admin, shift changeover, rostering etc over your whole fleet	less than 5 hours ☐ 5-9 hours ☐ 10-14 hours ☐ 15-19 hours ☐ 20-24 hours ☐ 25-29 hours ☐ 30-34 hours ☐ 35-39 hours ☐ 40-44 hours ☐ 45-49 hours ☐ more than 49 hours ☐
27) Office / miscellaneous expenses (phone, electricity, accountant fees, admin staff wages, rent, computers, etc)	$ ______ per month

28) Average cost of driver uniforms per vehicle per year	Less than $150 ☐ $150-400 ☐ $401-$650 ☐ $651-$900 ☐ $901-$1,400 ☐ $1,400-$1,900 ☐ $1,901-$2,500 ☐ More than $2,500 ☐
29) Do you pay your drivers sick leave pay or holiday pay?:	No ☐ Yes ☐ If yes, how much do you pay? $__________ per year **OR** _________ days per year
30) What type of payment arrangement do you have for drivers?	**% of fare revenue** ☐ What % do drivers get? _______% **OR** **Fixed pay-in** ☐ What is the pay-in? $___________ per shift
31) Average fare-taking per driver	$_________ per week **OR** Don't know ☐
32) In general, what shifts are driven by operator or a driver, and what revenue is taken per shift?	**Shift** **Driver** **Average Revenue** *Weekday (Mon-Fri)* Operator-driven shift ☐ **OR** Casual driver shift ☐ Revenue per shift $__________ *Week night (Mon-Thurs)* Operator-driven shift ☐ **OR** Casual driver shift ☐ Revenue per shift $__________ *Weekend day* Operator-driven shift ☐ **OR** Casual driver shift ☐ Revenue per shift $__________ *Friday night* Operator-driven shift ☐ **OR** Casual driver shift ☐ Revenue per shift $__________ *Saturday night* Operator-driven shift ☐ **OR** Casual driver shift ☐ Revenue per shift $__________ *Sunday night* Operator-driven shift ☐ **OR** Casual driver shift ☐ Revenue per shift $__________
33) What costs do drivers or operators pay based on their bailment agreement?	**Cost item** **Amount** **Who pays?** Basic wash / vacuum $_______ per week Driver ☐ **OR** Operator ☐ Fuel $_______ per week Driver ☐ **OR** Operator ☐ Administration expenses $_______ per week Driver ☐ **OR** Operator ☐ (e.g. time spent on paperwork) Other _________ $_______ per week Driver ☐ **OR** Operator ☐
34) Cleaning frequency	Never ☐ Weekly ☐ Monthly ☐ Quarterly ☐ Six monthly ☐ Annually ☐
35) Fuel use & cost	Fuel type: LPG ☐ Diesel ☐ Unleaded ☐ Last price paid $______ **/ litre** __________ **litres per 100km obtained**
36) Insurance	**Average policy cost per taxi for greenslip:** $_____ per year. **Average policy cost per taxi for comprehensive insurance:** $_____ per year. **Comprehensive excess:** $_______ **No claim bonus:** 20 ☐ 40 ☐ 60 ☐
37) Other cover	3rd party property ☐ Average policy cost per taxi $_____ p.a. Excess: $_______ Registration ☐ Average policy cost per taxi $_____ p.a. Workers Compensation ☐ Average policy cost per taxi $_____ p.a.
38) Any other cost items which may not be covered in the above	☐ Network Fees at $_________ per vehicle per year ☐ LPG Conversion at $_________ per vehicle

	☐ Wheelchair Accessible Taxi (WAT) Accessibility fitout (e.g. lift, additional meters) at $_________ per vehicle ☐ Roof bars, lights, signage, livery, meter, camera &/or shields at $_________ per vehicle ☐ Other (please specify)________________________________ at $______________ per vehicle ☐ **or** per year ☐ ________________________________ at $______________ per vehicle ☐ **or** per year ☐ ________________________________ at $______________ per vehicle ☐ **or** per year ☐ ________________________________ at $______________ per vehicle ☐ **or** per year ☐ ________________________________ at $______________ per vehicle ☐ **or** per year ☐ **Total $_____________ per year**

IF YOU ALSO DRIVE YOUR OWN TAXIS, PLEASE FILL OUT THIS SECTION BELOW:

1) About your last shift **If possible this information should be obtained from the meter.** **Please provide a copy of the meter printout if the meter has that facility**	**Date:____________ Time: from_________ am/pm to ___________am/pm** **Number of passenger trips provided: _________________(number)** **Number of radio bookings accepted (if information available): _____________(number)** **Number of kilometres travelled:___________________(kms)** **Number of booked kms:____________(kms)** **Number of kilometres travelled for which fares were generated: __________(kms) OR __________% of km** **Estimated waiting time: ____________(hours per shift)** **Odometer reading at beginning of last shift ___________(kms)** **Odometer reading at end of last shift ___________(kms)**
2) Use of toll roads (as compared to alternative routes)	**Frequency of use:** Never ☐ Rarely ☐ Regularly ☐ Always☐ **Percentage time saving per trip:** Less than 10% ☐ 11-20% ☐ 21-30% ☐ more than 30% ☐ **Do you usually use toll roads without passengers on the return trip?** Yes☐ No☐
3) Rank the following in terms of the frequency of the trips you make on average? **(from 1–most frequent, to 6-least frequent)**	2 kms or less __________ >2 – 5 kms __________ >5 -10 kms __________ >10 -15 kms __________ >15 -20 kms __________ Greater than 20kms __________