

# **Western Australian Tax Association**

**Submission to the Economic Regulation Authority**

in response to

**Draft Report**

**Inquiry into Microeconomic Reform in Western Australia**

May 2014

## **Overview**

The Economic Regulation Authority (ERA) has produced a draft report on its inquiry into Micro Economic Reform in Western Australia.

Amongst the economic sectors that the ERA analysed was the local taxi industry. The major finding from that work was to recommend the deregulation of taxi plate numbers but otherwise maintain government regulation over most other aspects of the industry, including price controls.

The West Australian Taxi Association (WATA) has reviewed ERA's analysis of the taxi industry and is suitably impressed by its quality and detail.

However, WATA notes that the analysis of the taxi industry and impact of ERA's proposals includes some unrealistic assumptions at critical points.

These over optimistic assumptions will influence the findings and consequent recommendations. WATA sees the expectations raised by the ERA of the impact on service and fares flowing from their proposed changes as more a hoped for result than something that will happen.

ERA must be mindful in its deliberations that they are proposing a radical change to a fundamentally efficient industry currently delivering millions of satisfactory taxi services each year and at the cheapest fares amongst Australian capitals.

On the contrary, WATA is greatly concerned that the radical recommendations to collectivise the taxi industry by turning it into a fully government owned taxi industry could result in an over all reduced quality of service, an outcome that neither the consumers nor the industry want to see.

Therefore, WATA urges the ERA to revisit its work on the taxi industry in light of comments from various industry participants, including our submission, and review its recommendations.

WATA will strongly urge the government to reject ERA's radical recommendations for the collectivisation of the taxi industry in order to ensure we maintain a viable private enterprise taxi industry delivering a reliable service with a high quality standard.

## **The ERA Report in Brief**

The following is a brief summary of the thrust of the ERA's report on the taxi industry:

- Abolish control over taxi plate numbers with the government issuing plates on demand.
- Taxi numbers will increase dramatically ahead of demand leading to reduced average taxi income.
- This will lead to greater competition between taxi drivers leading to more innovation and lower fares even though taxi drivers earn only a minimum hourly wage.
- Abolition of private taxi plate ownership will also result in lower fares by removing taxi plate costs.
- Taxi driver affiliation with taxi dispatch services should be voluntary.
- Taxi industry will otherwise remain highly regulated in all other aspects, including price controls.

WATA's response, in brief, is:

- ERA recognises the need for taxi industry regulation and it is driven by consumer demand for safety and a minimum standard in quality of vehicle and service.
- ERA's conclusions on the control of taxi plate numbers are based on analysis involving assumptions discordant with the economic reality of the industry.
- ERA has not given proper weight to the massive growth in taxi numbers over the past decade with the release of government taxi plates.
- The large number of peak period taxis is evidence that the taxi market is already well catered for, and particularly in terms of conventional taxis.
- A large increase in taxi numbers resulting in reduced income for drivers will cause even greater difficulty in driver recruitment and potentially a reduction of taxi services outside peak periods.
- ERA's recommendation will have other negative outcomes stemming from lower driver income such as falling driver and vehicle standards and taxi congestion at popular locations and taxi ranks, as has occurred elsewhere that such deregulation has been tried.

## **WATA's Response to ERA's Report on the Taxi Industry**

### **1. Taxi industry to remain highly regulated**

Government regulation of the taxi industry covers the number of taxis in industry, maximum price that can be charged for taxi service, the quality of taxis and the standards of conduct by taxi drivers.

The ERA does not find any comparable jurisdiction where taxis are completely deregulated and it recognises the necessity of retaining most of the current regulatory framework.

WATA notes ERA's implicit recognition that the taxi industry is not amenable to a minimal regulatory arrangement.

WATA has always understood that the demands of consumers for a certain minimum quality of taxis and maximum safety means that we will be a highly regulated industry.

WATA concurs with the findings that a considerable regulatory burden is a necessity that the taxi industry has to accept.

### **2. Need to regulate taxi and driver quality standards**

Current regulations set standards for the quality of vehicles operating as taxis to ensure passenger safety and uphold certain minimum quality standards for the benefit of passengers.

ERA acknowledge the need for such regulations as they ensure basic quality standards are maintained and give passengers assurance as to the quality and safety of taxis.

Removing such regulations would likely lead to a deterioration in quality of taxis and loss of confidence in taxi safety amongst the public.

Regulations setting out requirement for obtaining a taxi driver license are also deemed as a necessity by the ERA. Process of becoming a taxi driver involves the Taxi Aptitude Test, Taxi Driver Training Course and the Taxi Driver Registration Test. In addition, new legislation will soon introduce a points scheme similar to a driving license whereby drivers will be subject to points for minor errors but could find themselves out of a job if these minor problems are not addressed.

Setting regulatory standards for drivers carries a cost but it is one deemed by the ERA as a necessity to provide minimum standards of quality involved with the taxi service industry. It provides comfort and assurance to passengers about the driver having demonstrated the required driver standards.

WATA agrees with the ERA on the need to maintain regulations covering quality of taxis and taxi drivers.

### **3. Driver conduct regulations**

This is another arm of quality regulations dealing with the conduct of drivers covering fare acceptance, economical route taken and dispatch company affiliation.

Fare acceptance regulations require drivers to pick up any passengers subject to the exceptions relating to driver safety, passengers behaviour and concerns about payment. The requirement for the driver to take the most economical route is obviously a protection mechanism for passengers against excessive journey costs.

ERA agrees with the need for regulations covering the first two aspects as picking up all passengers is a social objective and the most economical route requirement means passengers have some confidence that they will not be over charged.

WATA concurs with those findings.

### **4. Dispatch company affiliation**

The ERA analysis concluded that there is no basis to justify the mandatory requirement for taxi drivers to be affiliated with a dispatch service provider.

The report notes that such requirements are based on the twin objectives of offering some sense of driver safety and providing universal access for passengers to all taxis. The report discusses the possibility of new technologies being able to provide both objectives without the regulatory need for taxi drivers to affiliate with a dispatch service.

The ERA does not present a convincing case for removing the mandatory requirement to affiliate with a dispatch service yet it nonetheless advocates for its removal.

If many drivers withdrew their affiliation in order to cut costs in the face of falling incomes, it would lead to a reduction in service quality. Many, if not most people would still use the dispatch service for calling a taxi but the number of taxis available through the service would be reduced. The result is a reduction in the availability of taxis and thus a reduced level of service, something contrary to ERA's objectives in promoting its reform ideas.

Such an outcome would also mean higher costs for drivers who remain with the dispatch service as much of its cost structure is largely fixed. This means more pressure for fare rises and would again produce an outcome contrary to that sought by the ERA's proposed reforms.

The ERA places much faith in phone technology being an alternative to dispatch company arrangements. Whilst phone technology undoubtedly can add a new dimension to taxi services, a proliferation of applications can create a fragmented taxi industry that means the public in general will not have a universal taxi service and particularly for the many people who are not technology savvy.

WATA does not support the recommendation to abolish the requirement for taxi drivers to affiliate with a dispatch service provider.

## **5. Price controls**

ERA states that there is less need for price regulation in an open market where anyone can readily obtain a taxi plate. However, it also recognises that even in the most competitive, deregulated markets there is some form of price regulation imposed to prevent taxi drivers taking advantage of regular peak demand periods and seasonal peak demand periods to obtain higher fares, or price gouging. It therefore states that some form of price regulation would be required even if taxi numbers became unregulated.

There is an inconsistency in the ERA's position on this point as it takes a view contrary to their basic principles and often stated belief that markets should be free to decide on price.

The ERA has built a reputation for pushing for free markets wherever possible, and that includes freedom for business to charge whatever it wants, constrained only by competition and consumers' willingness to pay higher prices. It is not clear why they should say that the taxi industry cannot be given the same pricing freedom as any other industry, and even the opportunity to get extra revenue in high demand periods like every other industry does. This is a critical flaw if the recommendation for deregulation of plates is expected to result in more taxis competing for business resulting in reduced incomes for all taxi drivers.

The current regulation system is designed to ensure that taxis generate sufficient income to entice people into the industry and generate a return for owners who have invested in taxis. Removing control of taxi plate numbers must be associated with the simultaneous removal of fare controls allowing taxi drivers and owners to generate a reasonable income and return on their investment.

WATA's view is that to contain fares, as the ERA wishes to do in response to price sensitivity of consumers, it has to be done with control over taxi numbers aimed at a balance between the need of consumers for marginal improvement against a need to ensure taxi drivers can earn their modest income.

Taxi drivers are already on minimum wages and faced with loss of income in a deregulated market, they should be able to improve their earnings in periods of peak demand with higher fares.

WATA does not support the retention of price controls in a deregulated market.

## **6. Deregulating taxi numbers**

This is the one area that the ERA strongly urges deregulation by the abolition of private plates and unrestricted release of new plates.

According to the ERA, current regulations create problems for taxi users. Changing the regulatory framework could produce lower fares, greater availability of taxis, more reliable and timely service, and greater product differentiation amongst taxi services.

It must be noted that the ERA's view that all these things "could" happen is not supported by evidence that such outcomes occur wherever control of taxi numbers was deregulated, which itself has not been done in many places.

The major reason for the ERA's conclusion that fares will fall relates to the cost of leasing plates which the ERA assumes would be abolished thus allowing fares to fall. This is based on the optimistic but unrealistic assumption that a large number of taxi drivers would be investing in a vehicle and associated costs to turn it into a taxi. Such an assumption ignores the transient nature of the taxi driver market in which many drivers, if not most, are not looking at taxi driving as a long term career but a short term job.

Drivers who do not want to invest in their own taxi would look to lease taxis on a shift basis, something taxi owners would welcome as they cannot drive 24 hours a day. The result will be a continuation of leasing costs for many drivers which would have to be reflected in the fare structure thus working against ERA's expected price fall.

ERA's analysis found that the cost of leasing a taxi plate in Perth, set by government at a maximum of \$355 per week, was around one third below Sydney and Melbourne costs that are around \$550 per week.

Lease costs are estimated to be about 16% of the total cost of taxis built into the fare model. This means that our lower plate lease costs are contributing to Perth having around the lowest taxi fares in Australia, despite this being recognised as an expensive city.

Studies examined by the ERA find that driver income remains roughly the same before and after deregulation. Such a finding means there is no financial benefit for drivers from deregulation. On the contrary, if there was a large increase in taxi numbers under a deregulated market, it will lead to lower incomes for drivers as there are more taxis competing for the same market. Under such circumstances, drivers will not be agreeable to cutting prices even if they were not paying plate lease costs.

The situation for drivers could be worse if deregulation did create enough competition for drivers to start competing on price by offering lower fares. Lower fares with reduced trip numbers means the current minimum wage earnings could fall below the minimum. This could be expected to create a situation where drivers focus on lucrative segments of the market at the expense of other segments thus reducing taxi availability to the community in general.

Reduced earnings can also be expected to diminish the number of new taxi drivers entering the industry which will only exacerbate problems with peak demand period and late night weekend demand. Reduced incomes for taxi drivers who are already earning a minimum wage will also make it even more difficult to lift driver standards.



## **7. Taxi market already saturated**

The ERA notes that the number of taxis increased by between 50% and 100% in some of the handful of places where deregulation was implemented and expects a similar outcome if taxi plate numbers were deregulated here.

The ERA has missed a critical part of recent history of the taxi industry with the release of hundreds of government leased taxi plates over the past decade that have saturated the Perth taxi market.

The issuing of government owned plates has seen taxi numbers increase by nearly 50% already. It will be most unlikely that the numbers would increase again by such amounts if the government deregulated taxi plate numbers.

Statistics in the ERA report show there are now more government leased taxi plates than privately owned.

The conventional taxi plate market (fulltime) has 984 privately owned conventional (full time) taxi plates and 618 government owned plates.

In recognition of the reality that the conventional taxi market was being saturated by growth in government issued plates, and that the mining boom had created a large but niche peak period demand, successive governments have put emphasis on peak period plates.

ERA report shows there are now 390 government owned peak period plates and only 22 privately owned. These peak period plates represent nearly 20% of the taxi fleet.

ERA's proposal to lift control over taxi numbers would first result in 390 peak period taxis converting to conventional taxis. That means demand for more than 400 extra full time drivers or up to 1,000 part time drivers. Any further growth would stretch the driver pool capacity to point where many taxi owners will only work peak periods and minimal conventional hours without leasing their taxi to other drivers. The outcome could be less taxis available during routine weekday hours.

The taxi owners would look to leasing fees as a means of generating a return on their investment in the vehicle and associated costs. After all, they would not be so charitable as to give their vehicle to others to generate an income and cause wear and tear of vehicle for free. Such fees will have to be recognised under regulated price model thus diminishing prospect of expected price falls in a deregulated market.

It must be recognised in any analysis of Perth's taxi industry that taxi plate numbers increased dramatically over the past decade in response to demand driven by unique economic circumstances in WA, specifically the mining boom we experienced. Those economic conditions saw a rapid rise in demand for taxis in peak morning periods, particularly for airport linked trips.

The growth in taxi numbers, including limited peak period taxis, has addressed the unique demand growth we experienced in Perth over the past decade and also helped address the excess demand that existed in the weekend night time peak periods. Now that we are back to steadier economic conditions, there is simply not enough work to sustain another massive increase in taxi numbers.

## **8. The Northern Territory and elsewhere experience**

Deregulation of taxi numbers was tried in the Northern Territory. The result was contrary to the theoretical expectations of those who advocated the case.

The Northern Territory experience is well documented in a paper by Prof Des Nichols of the Faculty of Economics and Commerce at the Australian National University.

The following captures the essence of the author's conclusions:

"As a result of this deregulation, the number of taxis increased dramatically with a resulting significant negative impact on driver earnings and service quality.

The taxi industry found that competition by taxi owners and operators to find drivers led to a lowering of standards. Prior to deregulation the majority of complaints related to length of time it took for taxis to arrive for fares. Following deregulation, the overwhelming majority of complaints related to driver standard, safety and driver incomes."

The paper highlights findings from other studies, including an analysis of international experience by C-H Kang that found:

"As a whole however, the effects of taxi deregulation were not so beneficial to consumers due to increased fares and deteriorated service quality. ... Therefore, this study concludes that market entry should be regulated somehow ... "

That study also found localised problems from excessive taxi numbers including congestion problems at places like airports and designated taxi ranks.

The paper further referred to work by PS Dempsey into the “collision of economic theory and empirical reality” which concluded that:

“In the final analysis, the suitability of taxi cab service and pricing is a peculiarly local issue, best tailored by local governments based on their unique populations, special densities, road congestion ... In this area, the state and local government should be left alone to foster the unique local public and private transportation system that suits them best.”

These passages reflect experience of others who have tried this approach and it shows a pure free market approach has not delivered on the theoretical expectations with respect to taxi services.

## **Conclusion**

WATA has outlined our reasoning for objecting to the radical reform proposed by the ERA to abolish market entry controls for new taxis and in the process collectivise and abolish privately owned taxi plates.

In essence, the market theory predictions will not be met, as they have failed to fully materialise anywhere they have been tried. We believe the adverse outcomes for industry and consumers will outweigh any marginal benefits in terms of waiting times at taxi ranks.

The adverse outcomes for the taxi industry in general, with declining taxi driver incomes particularly problematic, would be augmented by adverse impact on consumers with falling driver standards, falling taxi vehicle standards, possible decline in taxi services outside peak periods, and increased safety risks for drivers and customers.

The ERA should revisit its analysis of the taxi industry taking note of the reality that:

- taxi drivers are earning minimum wages and thus could not be expected to reduce their earnings further by lowering fares;
- any reduction in driver income as a result of more taxis sharing the work would see drivers exiting the industry and make it more difficult to attract new drivers;
- most taxi drivers would not be interested in investing in a taxi vehicle and thus there will continue to be a taxi leasing market with lease cost built into the fare structure;
- Perth has already experienced a massive increase in taxi numbers over the past decade that has saturated the market and met the excess demand that existed in peak periods and thus would be unlikely to see another large increase under a deregulated model.
- The adverse consequences experienced elsewhere must be given their due importance in advocating such an approach here.

Finally, as the ERA is not willing to support a pure market approach and let prices be deregulated, then the trade off for controlling prices has to be market entry restrictions to protect the incomes of those forgoing free market earnings.