

6 REVIEW OF FARE REGULATION

Introduction and summary

- 6.1 This chapter reviews the regulation of taxi fares. To assess the impact of fare regulation we:
- looked at the rationale behind fare regulation and the protection it affords consumers
 - considered the impact that fixing fares has on the market for taxis
 - took into account the experiences of international markets that have deregulated fares.
- 6.2 The research we commissioned to inform this assessment is at annexes D and J.
- 6.3 We have found that, whilst there are some arguments for removing fare regulation, the case for retaining controls is much stronger. The nature of the rank and hail sector of the taxi market makes it almost impossible for consumers to exercise choice on price as it is very difficult to shop around. Deregulating fares may therefore lead to higher prices. This is particularly important, for example for disabled consumers (who may not have access to alternative forms of transport), for those concerned about their safety (for example if they are catching a taxi late at night), or for those who do not know the local area. In these and other instances, fare regulation protects consumers from being overcharged.
- 6.4 However, there are measures that could be taken to introduce further competition on price into the market.
- 6.5 **We recommend that throughout the UK LAs should only set fare tariffs which represent the maximum that can be charged, and not set fixed or minimum fares. It should be made clear to consumers that they are able to negotiate on fares, for example, when ordering a taxi over the telephone. We also recommend that, where possible, LAs actively facilitate more price competition in the market, particularly in the rank and hail sectors of the market.**
- 6.6 This chapter looks at these issues and the background to the recommendations in more detail. Section 1 looks at the background to fare setting in the UK. Section 2 deals with the effects of these regulations on the market. Section 3 assesses a number of different

approaches to fare regulation and section 4 gives our conclusions and recommendations.

Section 1: background to fare setting

- 6.7 LAs can regulate fares for taxis but not for PHVs. Ninety-five per cent of LAs that responded to our survey regulate fares.
- 6.8 In England, Scotland and Wales outside of London fares set by LAs represent the maximum that can be charged¹²². This allows taxis to compete on price by offering lower fares to consumers. However only 25 per cent of those LAs responding to our survey make this clear on their fare tariff cards. In London, a mandatory tariff is set which does not allow taxis to give discounts to consumers on a regular basis.¹²³ In Northern Ireland the LA has the power to set both maximum and minimum fares, although in practice these are set at the same level, creating a mandatory tariff.
- 6.9 In those authorities where fares are set by the LA, taxis tend to use taximeters to measure the distance and/or time involved in a journey. This is often required by the LA as a licensing condition.¹²⁴ In England and Wales outside London PHVs may also use taximeters, but LAs cannot require them to do so. However, if they choose to use taximeters, these must be tested and approved by or on behalf of the relevant LA. There is no clear pattern of taximeter use by PHVs. Our survey of LAs found that in some cases the majority of PHVs have taximeters fitted whilst in others no PHVs have taximeters fitted.
- 6.10 LAs have no powers to set PHV fares.¹²⁵ Fares are set by individual firms or may be negotiated directly with customers. Our survey of LAs found no clear relationship between taxi fares and PHV fares. In some areas licensing officers report that PHV fares are significantly lower than taxi

¹²² This was established in the case of *R v Liverpool City Council ex p. Curzon Limited* 12 November 1993 CO/1338/91 QBD, unreported.

¹²³ Although they are allowed to depart from this tariff on occasion, e.g. if a passenger has had their money stolen. This judgement must be made on a case by case basis. There is no blanket discretion.

¹²⁴ This is not always the case. For example in Dumfries and Galloway the fare is calculated based on the distance shown by taxi's mileometer rather than using a taximeter.

¹²⁵ Apart from the Department of the Environment in Northern Ireland, which may set fares for PHVs as well as taxis but in practice does not do so.

fares, whilst in other areas it is common for PHVs to have taximeters fitted and to charge the same fares as taxis.

Fare regulation in practice

- 6.11 The process for setting taxi fares differs between LAs. Statistics from the DfT show that in 35 per cent of authorities surveyed, the fare tariff is revised following requests from the taxi trade, and in 65 per cent the fare is revised on a regular basis, in most cases yearly.¹²⁶
- 6.12 The decision-making process for changing fare levels also differs widely. In London, a formula for fare increases has been established, based on changes to driver and vehicle costs. Outside London the standard process in many areas is for representatives of the taxi trade to put forward a proposed fare increase to the local council's licensing committee, which is then either approved or rejected. The law requires that any change to the fare tariff must be published in a local newspaper and deposited for inspection at the council offices for a minimum of 14 days. This allows members of the public to complain if they are unhappy with the proposed change. Some licensing authorities go further than this and directly consult with the public through focus groups and citizens' panels to get their views about taxi fares.¹²⁷
- 6.13 Table 6.1 illustrates the wide variety of different taxi tariffs throughout the UK.

¹²⁶ Department for Transport: Taxi and Private Hire Vehicles in England and Wales, 2001-2002.

¹²⁷ For example this practice occurs in Bristol, where a citizens' panel was consulted about the current level of taxi fares.

TABLE 6.1: MOST EXPENSIVE AND LEAST EXPENSIVE TAXI FARES BY LICENSING AUTHORITY:

Most expensive			Least expensive		
1	Luton (Airport)	£6.00	1	Hartlepool	£2.70
2	Vale of White Horse	£5.30	2	Alnwick	£2.80
	Epsom & Ewell	£5.20		Bolsover	£2.80
	Hertsmere	£5.20	3	North East Derbyshire	£2.90
	London	£5.20		North Lanarkshire	£2.90
3	Caradon	£5.10	4	Berwick on Tweed	£3.00
4	Adur	£5.00		Sedgefield	£3.00
	Brighton & Hove	£5.00		Warrington	£3.00
	Maidstone	£5.00	5	Blaenau Gwent	£3.10
	Sevenoaks	£5.00		Inverclyde	£3.10
	Tunbridge Wells	£5.00		North Tyneside	£3.10
				Thanet (Broadstairs)	£3.10

Source: Private Hire and Taxi Monthly, November 2003, based on a standard two mile daytime journey (The average UK fare is £3.93).

- 6.14 The level of fares in each area is likely to depend on a number of local factors including the bargaining power of the taxi trade, the affluence of taxi users in the area and the costs of providing taxi services. There is no obvious geographical pattern to explain the above results. We also have no evidence to suggest that fare levels differ between LAs with or without quantity controls.

Section 2: regulating taxi fares for on-street and rank hiring

- 6.15 This section sets out the rationale for fare regulation for rank and hail. In doing so we present theoretical and empirical evidence that underlies the rationale.
- 6.16 The legislation governing PHVs prevents them from plying for hire on the street or at ranks, so this section relates only to taxis.

Do taxi fares need to be regulated?

- 6.17 Fare regulation is intended to protect consumers from overcharging by taxis. In the 1993 Green Paper on taxis, the DfT stated that 'the control of taxi fares is justifiable, if at all, only because the consumer of taxi services at ranks or in the street is in a peculiarly weak position, cannot shop around, and is very vulnerable to overcharging'.¹²⁸
- 6.18 There are two main arguments given in support of fare regulation:
- the structure of the market and the way it operates provides little incentive for price competition between licensed taxi drivers
 - to protect vulnerable consumers.

Lack of competition in the market

- 6.19 The way taxis are hired from the street and from ranks results in situations where there is little consumer pressure for taxis to compete on price.
- 6.20 Consumers hailing taxis from the street face high and uncertain search costs. Shopping around is not a realistic option. If they choose to turn down a taxi because it is too expensive the waiting time until the next taxi arrives is uncertain, as is the relative price and quality of the next taxi compared to the current one. Moreover, consumers cannot return to the original taxi if they cannot find a cheaper option. The first taxi that the consumer hails effectively makes a 'take it or leave it' offer, which the consumer has to assess with very limited information.¹²⁹

¹²⁸ Department for Transport: Taxis and Private Hire Vehicles: A Consultation Paper on the Future of taxi and Private Hire Vehicle Services in England and Wales, 1993

¹²⁹ See Diamond, P. (1971). 'A model of price adjustment', *Journal of Economic Theory* 3, p156-168. and Shreiber, C. (1975), 'The economic reasons for price and entry regulation of taxi cabs', *Journal of Transport Economics and Policy* 9, p268-279.

- 6.21 Similarly, when consumers hire taxis from taxi ranks they are generally required to take the first cab from the rank. On many ranks this is convention rather than necessity and could be changed, but on some ranks there is simply no room for taxis to pull out from the middle of the rank. Again there is no scope for consumer choice, and so no incentive for taxis to compete on price.
- 6.22 For price competition to occur, taxis need to be able to signal to consumers that they are cheaper and customers need to be able to exercise choice over which taxi they use. As described above, customers hiring taxis from ranks or in the street are usually not able to exercise choice. In contrast, when booking a taxi over the telephone consumers are often in a better position to shop around and find the best price.
- 6.23 Price competition is more likely to occur in situations where firm reputation and repeat business are important. For firms operating in the telephone booking sector the chance of repeat business is higher and taxi firms are able to increase future sales by lowering prices. In this situation price competition is more likely to occur.
- 6.24 Where firms operate in both the phone sector and the hail and rank sector, price competition in the phone booked sector can in theory translate into lower prices in the hail and rank sectors. This may occur where a firm has a recognisable brand and competition in the phone booked sector keeps prices low. Any temptation on the part of firms to increase prices in the hail and rank sector would be tempered by the risk of losing the low price reputation gained in the phone booking sector. However this effect is likely to be limited and there is no empirical evidence to support the theoretical argument.
- 6.25 Overall, the combination of the inherent nature of the on-street taxi service, the first in first out rule at ranks, high search costs and the weak bargaining position of consumers means that taxis operating at ranks and on the street are not constrained by the competitive forces which result from consumers shopping around. As a result there is an incentive to charge high prices in the absence of some form of fare regulation. Where taxis are booked by telephone the scope for consumers to shop around helps to constrain the prices taxis can charge.

Consumer protection

- 6.26 Fare regulation is particularly important for consumers in a vulnerable position where they are more susceptible to overcharging.
- 6.27 First, consumers such as disabled and older people are likely to be in an even weaker bargaining position than other consumers because they are less able to take alternative forms of transport. This means they may be liable to get charged even more than other consumers if fares were not regulated.
- 6.28 This problem also applies to consumers in particular vulnerable situations. For example, those trying to catch a taxi late at night who may be concerned about their personal safety will be in a particularly weak bargaining position and could be charged a high price by an unscrupulous taxi.
- 6.29 The second problem is that some consumers will simply be less well informed than others about the price of taxi services and alternatives to taxis and so will be in a weak bargaining position over the fare. Tourists are a good example of this type of poorly informed consumer.
- 6.30 In the absence of fare regulation, there is no mechanism that will prevent consumers in vulnerable situations being charged excessively for using taxis services.

What happens when fares are deregulated?

- 6.31 Ninety-five per cent of UK LAs responding to our survey who licence taxis also regulate taxi fares, so domestic evidence on fare deregulation is limited. There is some anecdotal evidence from those authorities that do not regulate fares which suggests that consumers are not being charged excessively for taxi services. However, these authorities are mainly in rural or semi-rural areas with the vast majority of work coming from telephone bookings. As explained above, this might have the effect of encouraging price competition.
- 6.32 There is some evidence on the effects of fare deregulation from countries and cities around the world that have deregulated taxi fares. The results of these deregulations are mixed and depend on a number of factors. These include local circumstances such as the structure of the taxi market, the level at which the fare was set prior to deregulation, and other regulatory changes that accompanied fare deregulation. For this reason, the results of fare deregulation outside the UK can only provide

an indication of the potential outcomes from taxi fare deregulation in the UK rather than a definitive answer.

- 6.33 The following, taken from our international study shows what happened in five countries that deregulated fares.¹³⁰ The effects of fare deregulation varied considerably between the five countries. In some cases deregulation has been a success whilst in others fare regulation has been re-introduced. This lack of a strong evidential base in support of fare deregulation is an important result in itself.

Sweden

- 6.34 Taxi fares were deregulated in Sweden in 1990. Fares increased initially in real terms but have since increased in line with inflation. The deregulation of fares coincided with the introduction of a 25 per cent value added tax on fares. The introduction of this tax distorted the immediate effect of price deregulation as a high proportion of the tax increase would have been passed on from taxi firms to consumers, so it is not clear whether the subsequent price increases were due to price deregulation or tax. In the years following price deregulation, fare increases have been smallest in large cities and greatest in rural areas. This may reflect a lack of competition in rural areas or simply higher costs associated with taxi provision in these areas which have been passed on directly to consumers.
- 6.35 Strict rules govern the information on fares that Swedish taxis must display. These include displaying the price of a standard 15 minute trip of 10km on the inside of the vehicle and also on the outside of the vehicle in lettering that is visible at least two metres away.
- 6.36 To encourage price competition between taxis, different ranks charge different fares and consumers can choose between ranks on the basis of their preferences about waiting times, fares and quality of vehicle.

¹³⁰ TOI: The Impact of taxi market regulation - An international comparison (annexe J).

New Zealand

- 6.37 In New Zealand taxi fares were deregulated in 1989. Fares have fallen in real terms in larger cities (by 15 to 25 per cent) while the results in smaller towns were ambiguous. The law requires that maximum fares must be registered with the Secretary of Transport and calibrated on the compulsory taxi meter. Individual taxis are free to set their own fares below this maximum. The fare must be displayed on the inside and outside of the vehicle.

Norway

- 6.38 Uniquely, taxi fares have been deregulated in some larger cities without any accompanying removal of entry controls. Where fares have been deregulated they have increased. Unlike Sweden and New Zealand fare deregulation has not been accompanied by strict rules about providing information on fares to consumers.

The Netherlands

- 6.39 In the Netherlands, since 2000, regulated fares instead of being fixed, have been set at maximum levels. Fares have risen. This is because the licensing authority has increased the maximum fare. Our study shows that there is some evidence of price competition occurring, based on reports of some taxis charging less than the maximum fare.

The United States

- 6.40 During the 1970s and 1980s, a number of US cities deregulated almost all aspects of their taxi services including fares. Following deregulation, fares increased in real terms in almost all cases and fare controls were subsequently re-introduced. Fare increases for street and rank hiring were greater than fare increases in the telephone booking sector. The effect was particularly clear in terms of increased fares at airport ranks.
- 6.41 It is not possible to draw overall conclusions from these international examples. It is clear that fare deregulation has in some cases led to increases in fares. However, it appears that strict requirements on fare setting and providing information to consumers may have contributed to the relative success of fare deregulation in New Zealand.

Potential problems of taxi fare regulation

- 6.42 Notwithstanding the benefits of fare regulation, it needs to be recognised that fixing fares at a particular level can cause problems in the way that the market works.
- 6.43 LAs have very limited information about the taxi market on which to base their fare setting decisions. In many areas of the UK, the taxi industry is highly fragmented so gathering information from firms difficult. If LAs set fares too low, this may lead to long queues of consumers waiting for taxis. If fares are set too high, this may lead to long queues of taxis waiting at ranks or cruising the streets looking for work.
- 6.44 Setting fixed taxi fares also reduces the scope for price changes to act as a signal for matching supply with demand as happens in a normal competitive market. Where fares are fixed rather than set as a maximum, the limited potential for taxi firms to compete on fares is removed completely. In the hail and rank sectors, price competition is likely to be very limited, but in others there is more scope for competition to occur. Examples are ranks that do not require the consumer to take the first taxi on the rank or areas where lots of cruising taxis make search costs lower.¹³¹
- 6.45 Furthermore, if taxis were allowed to charge higher fares at times of peak demand this would encourage more taxis to operate at these times. This would benefit consumers by reducing waiting times during periods of peak demand. LAs can help to reduce waiting times to some extent by setting peak and off-peak fare tariffs that encourage a greater supply of taxis at peak times and less at off peak times. Anecdotal evidence on this point comes from London where the Public Carriage Office and representatives of the Licensed Taxi Drivers Association have told us that recent increases in the fares tariff at night have encouraged more taxis onto the streets at these busy periods.

¹³¹ Halcrow: Impact of Taxi Regulation on Taxi Markets – Case Study (annexe D). For example, in Worcester passengers are not required to take the first cab from the rank. However there was no evidence that this leads to price competition among taxis.

Section 4: assessment of approaches to fare regulation

- 6.46 In arriving at our recommendations on fare regulation we considered the likely effects that would arise from different degrees of fare deregulation.

Full fare deregulation

- 6.47 A full fare deregulation option, where consumers negotiate fares with drivers, was rejected due to competition and consumer protection problems in the hailing and rank sectors as outlined above.

Partial fare deregulation

- 6.48 Another option considered was partial fare deregulation, which would involve taxi firms setting their own maximum fare tariffs and keeping maximum fares at that level for an obligatory minimum period. Firms would be required to display a standard sample fare so that it is visible outside the taxi. Partial fare deregulation has occurred in Sweden and in New Zealand. The strict rules on how companies set and display their fares protect vulnerable consumers from being over-charged.
- 6.49 Partial deregulation is only likely to be a success in areas where price signalling can be effective and where consumers can actually exercise choice (for example by not being forced to select the first taxi in a rank).
- 6.50 There are likely to be implementation problems with partial deregulation. For example if the law requires that all taxis display a standard sample fare for a three mile journey on the outside of the vehicle so that potential passengers can compare prices, taxis can set their tariffs so that the fare for a three mile journey is low but the fare for other journeys is higher. Consumers are therefore still faced with uncompetitive high fares for longer journeys. These problems could be overcome, but at a cost of making the information presented more complex and therefore less easy for consumers to understand.
- 6.51 For these reasons we do not recommend partial fare deregulation for the UK taxi market.

Setting the fare as a maximum

- 6.52 A third option is for LAs to continue setting fares, but instead of setting a mandatory fare that all taxis must charge, the fare should become a maximum and taxis could choose to charge below this maximum.¹³² This will facilitate price competition in the limited number of circumstances where consumers are able to exercise choice. As described above, these include ranks that do not require customers to take the first cab on the rank and areas with a lot of cruising taxis where search costs are lower.
- 6.53 In its 1993 Green Paper on taxi licensing, the DfT concluded that all taxi fares should be set as a maximum rather than a mandatory tariff and that this should be made clear to consumers. The current situation, where not all LAs make it clear in their tariff that the fare is a maximum, is confusing for consumers and is likely to reduce price competition. Only 25 per cent of the LAs that responded to our survey publish a fare tariff that clearly states the metered fare is a maximum – in the other 75 per cent there is no mention of the fact that taxis can charge less than the published tariff.
- 6.54 A potential argument for not allowing taxis to set prices below the published fare is to prevent price competition driving out competition in terms of quality or safety. However evidence from the PHV sector does not support this argument. In the PHV sector prices are not regulated and a wide variety of fare levels and quality levels co-exist, from high-priced chauffeur-driven executive cars to cheaper discount cabs that simply meet the minimum standards required by law. Furthermore, we consider that quality and safety are best controlled directly, through the setting of minimum standards that taxis and drivers must meet.

Section 5: conclusion and recommendations

- 6.55 There are arguments both in favour of and against fare regulation for taxis. The nature of the market means that consumers, particularly vulnerable consumers, derive greater benefit from the existence of fare regulation. Fare regulation protects consumers.

¹³² This is theoretically already possible in the UK except for London and Northern Ireland.

- 6.56 UK LAs should continue to regulate taxi fares. However, there are some measures that can be undertaken to improve competition in the licensed taxi market whilst retaining the benefits to consumers of fare regulation.

Recommendations based on this assessment

- 6.57 **We recommend that throughout the UK LAs should only set fare tariffs which represent the maximum that can be charged, and not set fixed or minimum fares. It should be made clear to consumers that they are able to negotiate on fares, for example, when ordering a taxi over the telephone. We also recommend that, where possible, LAs actively facilitate more price competition in the market, particularly in the rank and hail sectors of the market.**
- 6.58 It is for LAs to decide how this might occur. One method used in other countries involved taxis displaying their fare in the window or the outside of the cab, either in terms of the price for a standardised trip, or a percentage discount off the metered fare.