THE TALE OF TAXI REFORMS IN TWO CITIES:
THE FAILURE OF CLOSED ENTRY - CONTINUED

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Introduction

The fight to enter the taxi market in parts of Canada and elsewhere in the world by Transportation Network Companies (TNCs), like Uber, continues. Uber is still unable to break into the BC taxi market and there will be no new taxis on Vancouver streets until at least Oct. 2017. In Europe, a report published by the OECD in May 2016 states 'The rapid rise of commercial transport apps such as Uber or Lyft is challenging long established rules in the for-hire passenger transport market. These platforms often fall outside existing regulations and governments have typically reacted by seeking to block them or by tweaking existing taxi regulation to include such services.'[1] The report goes on to state 'Oversight tends to be tilted in favour of established providers - often because of the specificities of street hailing, but also due to market capture.'[2]

This paper continues our description of the regulatory developments in the taxi industry in Toronto and Ottawa. The first section summarizes our earlier paper. The next section presents the taxi industry response to competition. Then the new regulations that were adopted by Toronto and Ottawa are described. The concluding discussion addresses the purpose of such economic regulations.

The Tale of Taxi Reforms in Two Cities: The failure of Closed Entry – Summary [3]

Toronto: Changes in the issuance of new taxi licences (i.e. based on the taxis owned) in 1974 led to a dire situation (with regard to regulation and service). Against this background, the Emergency and Protective Services Committee Council established a Task Force to Review the Taxi Industry. The Executive summary stated "The creation of this Task Force was the culmination of a number of recent articles in the media and the concerns expressed by the public, taxicab owners and drivers, Toronto Licensing, the Board of Trade and the tourism industry respecting the state of the taxi industry in Toronto." On October 1998, the Task Force released its report. A second review was undertaken in January 2014 and a third in September 2015.

In response to the 1998 report the City of Toronto made changes to improve the quality of vehicles and drivers such as age limits on vehicles and mandatory driver's training for new licensees. The most important recommendation that it adopted was with regard to a new class of licences known as 'Ambassador' taxis. Its current by-law permits it to issue up to 100 Ambassador licences each year, in addition to the granting of accessible licences. Further studies were undertaken to establish criteria to be used in determining supply of taxis.[4] This action was to greatly diminish the risk of any taxicab serving the public and tourists, while in dangerous and unsafe condition." [5]

In response to the 2014 report the important changes made by the City were: creation of a new licence (the Toronto Taxicab Licence (TTL) which is owner-operated, transferable and accessible); direction to issue 290 new taxicab licences to ensure accessible taxicabs for the Pan Am Parapan Am Games; permission to transfer Ambassador taxicabs (i.e. sale); operation of hybrid, low-emission or alternative fuel vehicle taxicabs (excluding those that are wheelchair accessible); permission for hybrid, low emission, alternative fuel and accessible taxicab vehicles to be 7 model years old; and consideration of changes regarding inspections, insurance and rates of operation.

In response to the 2015 report nine recommendations were made. The most important are: amending the definitions of taxicab broker and limousine service company to ensure that all technology-based brokerages are captured within the current regulatory regime; dropping the cost to enter the taxicab from $4.25 to $3.25 (i.e. the drop fee); reviewing the Taxicab bylaw with a view to reducing regulatory burden and increasing competitiveness; addressing the 23 outstanding City Council and Committee taxicab directives; reviewing the Limousine bylaw with a goal to update and modernize, while also considering the appropriate level of regulation and the interest of the public; and directing staff to undertake the development of regulation that would permit private vehicles-for-hire, including UberX, to operate (subject to proof of the availability of adequate insurance).

The recommendations of the 1998 report ultimately led to a new By-Law in 2001, the recommendations of the 2014 report led to By-Law 503-2014 and the 2015 Report led to the new regulation A New Vehicle-for-Hire Bylaw to Regulate Toronto's Ground Transportation Industry (LS10.3). The latter is discussed subsequently under the section New Regulations: 2016.

Ottawa: In 2000, the taxi industry was in a state of decline as a result of enforcement of artificial zones, the limit on the number of taxicab licenses (resulting in escalating plate values), and aging taxicabs. Against this background the Taxi Project Team was set up to evaluate the situation. Its initial report endorsing open entry led to considerable controversy, protest and demonstration. On December 5, 2000, the Taxi Project Team released a final report in which it abandoned its option of open entry. The City then commissioned a report by KPMG that made a total of 38 recommendations. The City of Ottawa adopted many of the recommendations of the KPMG report including retaining control of supply of taxis but easing entry of new licensees through the Ambassador system as implemented in Toronto. However, cab licences were to be issued to a maximum of one per 540 city residents. It also accepted phasing in of the boundary elimination that would ultimately have the effect of being one zone. This led to a new By-Law in 2000.

In May 2015, the City hired KPMG to review the taxi regulations. KPMG and its assistants Mowat Centre, Hara Associates and Core Strategies Inc., released its report *"City of Ottawa Taxi and Limousine Regulation and Service Review"* on March 31, 2016 indicating that the status quo is not the answer. It made three suggestions: establish a new licensing category for app-based services, such as Uber; reform the current taxi system to include features present in Uber, such as driver rating, app-based credit card payment and reduced fares; and do away with the limit on the number of taxi licence plates. The recommendations of KPMG were considered in the city's staff report and based on the recommendations of the Committee (Community and Protective Services) the City Council passed a new regulation in 2016.

A review of the regulatory developments in the taxi industry indicates that shortly after 2014, the appearance of TNCs (transportation network companies) and entry of UberX created new problems for the taxi industry and for the regulators. Our earlier paper indicated that the evidence on price, service, entry and public reaction indicates that closed entry has failed to serve the interests of the public. The developments that have occurred since then are described hereafter.

Taxi Industry Response to Competition: Exclusionary Strategy

a. Media Reports

The response of the regulated taxi industry to the entry of competition called for immediate exclusion of their competitors. The fight between the taxi industry and Uber was intense and lasted for several months both in the streets and elsewhere. The following headlines should provide ample evidence of this: *TTA (Toronto Taxi Alliance) Thanks John Fraser For Anti-Uber Bill*; *Tip line to report Uber drivers to the Insurance Bureau of Canada*; *TTA thanks Justice Dunphy at close of Uber court hearing* (the injunction by the City was not granted by Justice Dunphy); *In the Uber vs. taxi industry mud-slinging, everyone looks dirty; Taxi industry to City, police: enforce the law*; *CDN$400M Class Action Commenced Against Uber X and Uber XL on Behalf of all Taxicab and Limousine Drivers, Owners and Brokers Licensed in Ontario, July 23, 2015*; *Toronto Cabbies go on Hunger strike against Uber; Recap of the Ottawa city council debate on legalizing Uber* ; *The Uber controversy reveals the rottenness of the taxi industry*; etc. The last article states ‘‘Taxi drivers oppose Uber because they are losing their customers. For those drivers who do not own a taxi permit, the decline in clientele further erodes their already limited income. For those drivers who do own a permit, they are victims of a double-edged sword: a declining customer base and a free fall in the value of the permit, which they purchased at the full price. … There is now an ongoing war of taxi drivers and cab companies against Uber. We've seen demonstrations, road blockages, intimidation and violence. But at root, both Uber drivers and traditional cab drivers all want the same thing: to support themselves, feed their families and pay their debts.” [6]

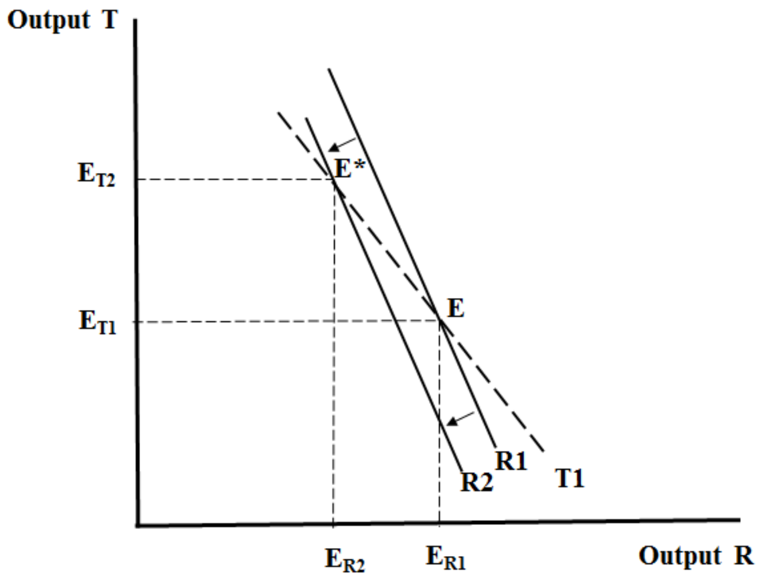
In sum, the taxi industry wanted TNCs made illegal because it would adversely affect their incomes and their wealth as represented by the value of the taxi licences. It called for the regulators to raise rivals cost and to reduce their revenue to see if its exclusionary strategy would succeed. In some cases, it worked as can seen when UBER stopped service in Edmonton for nearly four months when the city passed a bylaw compelling drivers to have proper commercial insurance (which it considered too expensive). They later entered the market but said that provincial licensing creates unnecessary barriers and will mean less flexible earning opportunities and less urban mobility. Similar sentiments were shown in Toronto when it was reported that ‘‘Ride service Uber is threatening to leave Toronto if the city passes new transportation regulations early next month, a move it says will leave 15,000 full-time and part-time drivers out of work. The company sent a letter to its Toronto users this week, making it clear it plans to shut down in the city if council passes proposed new transportation regulations. Uber objected to rules such as a proposed ban on cars older than seven years, and to a one-time $20,000 licensing fee.” [7] The regulators were caught in the middle: the need to serve the public’s demand for TNC service and the need to protect the taxi industry by creating a level playing field.

The latter was accomplished by raising TNC’s cost and reducing its revenue and enabling the taxi industry to reduce its cost and raise its revenue.

b. Raising Rival’s Cost - Reducing Rival’s Revenue

The concept of raising rivals cost - a tactic or device to gain market share or exclude competitors – gained popularity in the mid-1980s, with the work of Steven Salop and David Scheffman. Its origin however has been attributed to Professors Aaron Director and Edward H. Levi of the University of Chicago Law School, who wrote in 1956 that a firm with monopoly power can decide to impose additional costs on others in an industry for exclusionary purposes. They stated that such a tactic "might be valuable if the effect of it would be to impose greater costs on possible competitors." Analytically the decision that raises the rival’s cost has exactly the same effect as one that lowers the rival’s net revenue. The economic analysis that illustrate how such devices have an exclusionary effect is often shown in a duopolistic or oligopolistic setting using reaction functions. Church and Ware indicate that ‘‘In an oligopolistic setting, if one firm can strategically increase the costs of a rival firm its own price and profits will increase. … The same is true for a dominant firm facing a competitive fringe where the dominant firm can take action to increase the costs of the fringe firm." [8] While the taxi market has many firms, as a regulated cartel it competes with the TNCs as a duopolist.

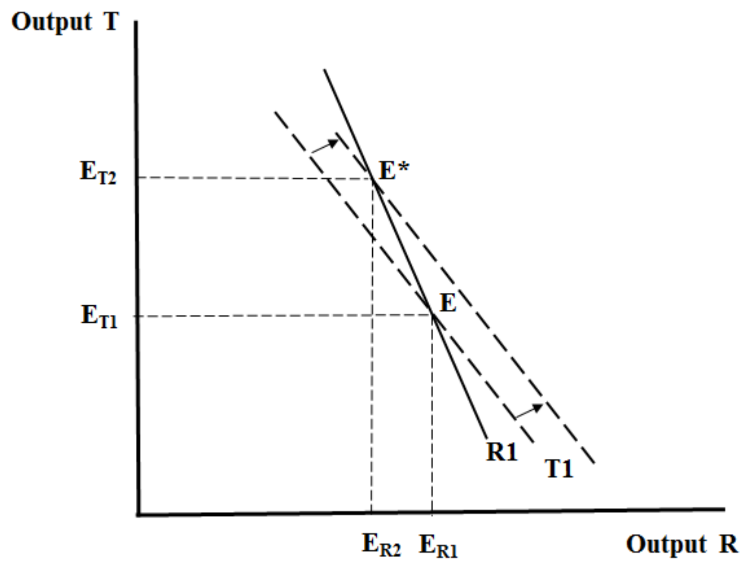
The economic model is constructed using the quantity of taxi output and the quantity of TNCs output. Suppose they are inversely related (i.e. the quantity of the taxi industry output (T) falls as the TNCs quantity (R) goes up and vice versa), further the two different quantity curves of the taxi industry (T1) and the TNC (R1) imply they have different costs.



Initially, the two curves intersect at point E. Here, the quantity of the Taxi industry output shown on the vertical axis is E_{T1} and the quantity of the TNC on the horizontal axis is E_{R1}. Suppose the Taxi industry succeeds in raising the costs of the TNC (or getting the regulators to do so) by shifting the quantity curve of the TNC leftward (R2). Now the two curves intersect at point E*. At this intersection, the quantity of the Taxi industry output on the vertical axis is E_{T2} and the quantity of the TNC on the horizontal axis is E_{R2}. It can be clearly seen that the E_{T2} is greater than E_{T1} and E_{R2} is less than E_{R1}. Further, if it is pointed out that any quantity sold by the TNCs less than E_{R1} will make it more difficult for it to stay in business then it becomes apparent why the taxi industry would want to raise its rival cost (or TNC cost). Examples of raising TNC costs are: imposing minimum insurance, requiring new model cars, imposing licence costs and fees, requiring safety inspections, etc. Examples of reducing TNC revenue are: prohibiting services except those booked through apps, prohibiting service to roadside hailers, raising minimum fare, remitting a fee per ride, etc.

c. Reducing Taxi Cost – Raising Taxi Revenue

Reducing taxi cost and raising taxi revenue have a similar effect as can be seen in a similar diagram below. Reducing its cost or raising its revenue results in the intersection at E*, in other words T1 moves to the right. At this intersection, the quantity of the Taxi industry output on the vertical axis is E_{T2} and the quantity of the TNC on the horizontal axis is E_{R2}. It can be clearly seen that the E_{T2} is greater than E_{T1} and E_{R2} is less than E_{R1}. Examples of reducing taxi costs are: requiring no refresher courses, removing certain fees, reducing licence fees, etc. Examples of increasing taxi revenue are: reducing meter fares (to compete with the TNCs), allowing rides booked through apps via the brokerage and providing for flexible pricing, etc.



In summary, the cities attempted to resolve the entry of TNCs by creating more regulations and by creating a situation they believed to be a level competitive playing field. These regulations are described hereafter. But was this a more optimal situation. Councillor Gord Perks, remarked "There's a more level playing field between the millionaires and the billionaires, but for the consumer, the level playing field goes down. The drivers lose, the public lose, the billionaires and the millionaires win. That's how this city has decided to apportion the benefits of new technology."[9] Tracey Cook, the head of city licensing, said some people were interpreting a “level playing field” between Uber and taxis as one that prevents competition. “The level of the playing field depends on the viewpoint you’re standing from,” Cook told council. “Many people’s view in the taxi industry of a level playing field means the same playing field and that there is no room for anything outside of taxicab service.” [10] The notion of managing competition and making competitive playing fields level hardly inspires confidence.

New Regulations: 2016

Toronto: On May 3, 2016, the City of Toronto passed a new regulation *A New Vehicle-for-Hire Bylaw to Regulate Toronto's Ground Transportation Industry* (LS10.3) to govern for-hire ground transportation. [11] The regulation has 101 sections and went into effect on July 15, 2016. The most important feature of the new regulation is that it introduces a new class of licence called private transportation companies (PTCs) that permits a ride to be booked for compensation through a smartphone application (section 2 and 3). Several conditions have to be satisfied before such rides are permitted. The most commonly cited are: PTC drivers must hold $2 million in liability insurance and provide proof to the city (section 24); PTC drivers must obtain a licence from the City and satisfy certain requirements and a PTC must maintain certain records and checks (sections 7 and 8)); PTC Vehicles pass mechanical inspections at City-run facilities, use Ministry of Transportation Safety Standards Certificates and related requirements (section 35); PTC vehicles can be no older than seven model years (section 31(d)); and PTC drivers will charge a minimum fare price — $3.25 and ensure a record is maintained that the passenger accepted the unregulated rate prior to the trip commencing (section 26). In addition, PTC drivers will add a 30-cents-per-ride charge to the fare price to be remitted to the city, pay an annual $15 per-driver fee and the PTC company will pay a one-time application fee of $20,000 (section 71).

The new regulation also brings about changes for the taxi industry that will reduce or remove the competitive advantage of new PTC entrants. The most important changes are: elimination for taxi drivers to take a 17-day initial training program and refresher courses together with the requirement for CPR and First Aid certification (sections 57 and 58); and permission for taxis to discount fares from regulated meter rates, and charge higher rates than meter rates if trips are booked through a smartphone (section 39). These regulatory changes will enable the taxi industry to reduce costs and to provide greater flexibility in pricing.

Ottawa: On April 13, 2016, the City of Ottawa passed a new regulation *Vehicle for Hire By-law* (By-law 2016-272) to govern for-hire ground transportation. [12] The regulation has 184 sections and went into effect on October 30, 2016. The most important feature of the new regulation is that it introduces a new class of licence called private transportation company (PTC) that permits a ride to be booked for compensation through an app. Regulations specifically pertaining to PTCs are contained in Part IV of this regulation (sections 132 to 148). Several conditions have to be satisfied before such rides are permitted. The most commonly cited are: a PTC must have minimum $5 million in Commercial General Liability and $2 million motor vehicle insurance and PTC drivers must hold $2 million in liability insurance (sections 140 and 144); A PTC vehicle must satisfy certain safety requirements, eg. Ontario Ministry Safety Certificate or alternative, annual safety check for vehicles less than five years and bi-annual check for vehicles more than five years (section 147 (1)(a)); PTC vehicles can be no older than ten model years (section 147 (1)(c)). In addition, the PTC will be required to remit to the city a charge of 11 cents per ride and will pay an application fee of $807 (1-24 vehicles), $2469 (25-99 vehicles) and $7,253 (100+ vehicles) (Schedule A – Fees).

The new regulation also brings about changes to modernize how it governs taxi drivers and brokerages together with loosening the rules for traditional taxi drivers aimed at allowing everyone to compete on a level playing field. The most important of these are: eliminating the $820 Algonquin College taxi course for drivers; allowing vehicles to be no older than ten model years (section 78(d)) instead of eight; eliminating the $1.50 service fee for customers paying with credit and debit in taxis; reducing the taxi licence fee by 43.5 per cent (i.e. to $96 from $170) (Schedule A – Fees), and eliminating it altogether for drivers of accessible taxis (Schedule A – Fees); and allowing taxi drivers to offer reduced fares, but only when pre-arranged through an app (section 90).

In sum, the new regulations will undoubtedly continue to be fine tuned after the cities study the impact of the existing PTC and when new PTCs enter the market.

Discussion

The legitimacy of entry restriction (or control over the number of licence plates issued) in the taxi industry is not new. The recommendation to restrict entry can be traced to the first official Report of the Industry n 1932. Its legitimacy was later embodied in the Statutes of Ontario. See 1954 An act to amend The Municipal Act, c. 56 s. 25.(1) which states "By laws may be passed by the council of towns, villages and townships and by boards of commissioners of police of cities: 1. For licensing, regulating and governing ... owners and drivers of cabs … for limiting the number of cabs ... used for hire, or any class or classes thereof;". And most recently in the City of Toronto Act, 2006 s. 94(1)(c) which states a by-law may "limit the number of taxicabs or any class of them." It is worthwhile noting that the clause "for limiting the number of cabs ... used for hire," was not in the 1950 statute Municipal Act (RSO 1950 c. 243 s. 406). With the formation of the Metropolitan Licensing Committee in 1953, it assumed control over the number of licences issued together with other matters and has maintained control since then.

The rationale for economic regulations that were concocted 85 years ago have been lost in time. A search of these documents provides no clear-sighted reason. Defenders are quick to employ such phrases as the "public interest" and "consumer interest" but nowhere are such terms defined. Clearly certain regulations are needed to serve the interests of the public by ensuring their safety and protection. Thus, there can be hardly any disagreement with Dempsey's conclusion that the fundamental question is not whether taxis should be regulated but how they might best be regulated. [13] The new regulations are designed permit the entry of new services that satisfies the demand of the public, while providing protection for the existing taxi industry.

The unanswered policy question is whether or not regulations to control supply and indirectly prices and a reasonable return on investment are necessary or appropriate. The economic regulations of the other transport sectors were removed because they did more harm than good. One of the risks of economic regulation that leads to the capitalization of licences is that the holders of these "rights" can see their value completely disappear if regulations change. Some may argue that the taxi drivers should be compensated in some fashion, but no justification exists for offsetting the loss of their economic rents. Posner [14] ruled in a court case of the Milwaukee taxis "The plaintiffs' [taxis] contention that the increased number of permits has taken property away from the plaintiffs without compensation, in violation of the constitutional protection of property, border on the absurd. Property can take a variety of forms, some of them intangible, such as patents. But a taxi permit confers only a right to operate a taxicab (a right which, in Milwaukee, may be sold). It does not create a right to be an oligopolist, and thus confers no right to exclude others from operating taxis." Licencing regulations that limit supply create economic rents that become capitalized over time. The recent entry of a new type of service is creating chaos for taxi licence owners in Canada because these capitalized rents are threatened with significant devaluation. The owners logically fight any change to the status quo, no matter what improvement might be possible to serve consumers better.

New ideas and new methods have so often called for new men and new institutions. "It was not the stage coach owners who built the railroads, nor the owners of fleets of clippers who developed the steamer … Nor did the railroad magnates promote the automobile. …the automobile magnates did not become airplane pioneers." [15] The taxi industry has constant returns to scale. The costs of the driver and car do not decline as more vehicles and drivers are added to the fleet. Some network economies are available through better information, and this is really the TNC's contribution. They can efficiently dispatch the closest car, centralize accounting and spread general overhead costs. The problem for the regulated taxis is that they have been sheltered from the need to evolve with the Internet Age. With superior information, the TNCs can vary prices according to demand. During peak demand periods, the TNC can raise prices to allocate demand (so-called "surge pricing"). During the off-peak, the TNCs can charge less than the regulated taxis and still be profitable. An industry so challenged by technological innovation has a simple choice: adapt or die. The problem they cannot control is the continuation of existing regulation.

Given the recent developments, in Toronto and Ottawa it is unlikely that deregulation is likely to happen in the near future unless the taxi industry feels that economic regulation no longer benefits it with the entry of TNCs. In the meantime, it may be worthwhile keeping track of the ongoing research in this area. A recent OECD report in this area states "…four principles emerge that should inform thinking around regulatory reform of for-hire passenger transport: Focus on the needs of consumers and society ... Keep the regulatory framework simple and uniform …

Chose innovative and flexible approaches to regulation … Use data-led regulation to improve benefits for all. [16]

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