

TAXI DEREGULATION: THREE YEARS ON

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Approximately three years have passed since deregulation in the Dublin taxi market. In this paper, Jennifer Daly demonstrates how the taxi market has changed since deregulation to benefit the consumers. Although increased benefits to consumers are confirmed by the research, the author warns about the possibility of regulatory recapture and calls for further liberal reforms in the market.

According to the theory of W.J. Baumol, a contestable market is one in which there is complete freedom of entry and exit for firms:

“It is a requirement of contestability that there be no cost discrimination against entrants. Absolute freedom of exit...is one way to guarantee freedom of entry...any firm can leave without impediment, and in the process of departure can recoup any costs incurred in the entry process” (Baumol, 1983)

This characterisation of a contestable market represents the very antithesis of the regulated Dublin taxi market up until November 2000. The idea of a contestable market approximates the ‘ideal’ perfectly competitive market outcomes by ensuring that the possibility of new entrants to the market disciplines the incumbents in the market to behave optimally.

Just over three years have passed since the High Court decision by Mr. Justice Murphy led to the removal of entry restrictions in the taxi market. Sufficient time has passed to determine whether the deregulated market represents a closer approximation to Baumol’s contestable market and also the positive and negative aspects of the change. Ultimately, I would like to establish definitively, whether deregulation has led to a significant improvement in services, and also, the implications of taxi deregulation for other transport sectors in terms of privatisation policy, e.g. the proposed privatisation of some of the Dublin bus routes and the proposed shake up of the Aer Rianta company.

Up until 1978 there had been no restrictions in the number of taxis allowed to operate in Dublin. In the period prior to regulation, increased demand for taxis led

to a significant increase in the number of participants. Incumbents, fearing oversupply lobbied the government and forced it into a position of 'regulatory capture' whereby entry was restricted, safeguarding incumbents earnings potential. As a result of this action, in the period up until 2001, the number of taxis operating in Dublin increased only marginally. The intervention in the market disrupted the 'free hand' of the market to allow supply of taxis to be determined by demand. As a consequence, a number of negative externalities arose in the intervening years.

According to the 1998 Goodbody report (Faber, 1998) on the taxi and hackney services in the Dublin area, taxi licences acquired a scarcity value and a secondary market was established whereby taxi licences traded for c. IR£90,000 and above. This was as a direct result of entry restriction, taxi licences themselves were merely a permit to operate and should not have had any significant value in their own right.

From the consumer's perspective, the results of market regulation were mostly negative. The limitation of entry placed a restriction on taxi supply at a time when demand was growing considerably. The growth in demand was due to a number of factors:

- Population growth: Between 1991 and 1996 for example, the number of adults residing in Dublin City and county rose by 10,000.
- Tourism growth: Tourist numbers also grew considerably, in the period from 1978-2000, the numbers of overseas visitors to Dublin grew from 2 million to 6 million each year (Barrett, 2003)
- Economic growth: Between 1985 and 1990, GNP grew by an average of 3.6% per annum. The arrival of the Celtic tiger in the mid-1990s brought a period of prosperity to Ireland. In the period from 1990-1997, GNP grew by an average of 5.6% per annum. Further economic developments meant that between 1991 and 1996, employment in the Dublin area grew by c. 65,000 (Faber, 1998).

These effects, together with a tightening of the drink-driving laws (Fingleton, et al., 1997) at the time translated into a significant increase in demand for taxis in terms of new users and also an increase in the frequency of travel by existing users. These effects led to a notable shortfall in taxi supply, which was estimated in the 1998 Goodbody report to be in the order of 2000 units, however, this may have been a conservative estimate.

This shortfall reflected unfavourably in the service available to customers. Waiting times at taxi ranks in excess of 90 minutes were not uncommon at peak

times. Also, 75% of people surveyed on street at the time felt that taxis were not easily available at peak times. In a similar vein, 46% of calls to cab companies led to wait times in excess of 20 minutes, while some calls were unable to secure a pick-up within a reasonable period. The overall customer perception from the study was that there was a lack of available cabs (Faber, 1998).

There appears to have been little reasoning for the 1978 regulation policy. General economic rationale for regulating entry may be based on a number of possibilities:

- Imperfect competition may result in a level of entry above that which would be socially optimal.
- A tendency towards inefficient entry may occur.
- Restrictions on entry may be used to correct for market failures other than excess/inefficient entry (Competition Authority, 2002).

In the first two cases here, it is probable that the regulator would not possess all the information necessary to determine which effect dominates and to be able to observe changes. We must not neglect the fact the regulation causes its own inefficiencies particularly in a situation in which incumbents are allowed to influence the regulator. The Competition Authority's report (2002) suggests that "regulatory capture is the most likely explanation for the quantitative restriction placed on taxis between 1978 and 2000". This indicates the possibility that the decision to regulate was not for consumer benefit, but rather reflected the preferences of vested interests, namely, the taxi drivers themselves. Furthermore, as regards the third rationale for entry regulation above, evidence from the 1998 Goodbody study indicates that restriction of entry has not altered firm behaviour in a socially optimal way (Faber, 1998). The Competition Authority goes further by stating that, as a mechanism for correcting market failures; entry regulation is a "blunt instrument" going on to say that there are "no convincing economic rationales for placing quantitative restrictions on the number of operators in taxi markets".

The 21st of November 2000 signalled a change in the awarding of licences. A high court decision by Mr. Justice Murphy on the 13th of October taken by hackney drivers Humphrey and Others against the Minister for the Environment and Others led to a removal of entry restrictions in the taxi industry. The action by Humphrey et al. questioned the decision taken by the Minister for the Environment and Local Government to increase the supply of taxis in Dublin by awarding an additional taxi licence to each existing licence holder. The judgement by Mr. Justice Murphy indicated that such a policy would be discriminatory and contrary to EC Treaty rules, in that it would restrict new licence holders to those mainly Irish nationals who were already operating. The decision by Justice Murphy stated: "any suitably qualified individual may provide taxi services". It was also stated in the

report that “regulations which restrict the number of public hire vehicles contradicted the very concept of public service” (Murphy, 2000).

The subsequent removal of entry restrictions led to an immediate increase in the number of taxis operating around the country. Taxi representative bodies responded by organising strikes and demonstrations opposing the decision to deregulate. In this instance, the government did not bow to industry pressure. The Taoiseach asserted at the time that “there can be no change in the government’s position on deregulation”.

The persistence of the policy of regulation of the taxi industry for a period of 22 years indicated the strength of the tendency of the government to protect incumbents. In its 2001 report, the OECD stated: “policy must move away from emphasis on protection of incumbents against innovation and competition”.

The report was also critical of government efforts in this area stating: “the coming cycle in Irish Economic Development justifies a more coherent and determined approach to regulatory reform than seen to date” (OECD, 2001). The 2000 deregulation policy was one step towards a “more determined approach” on the part of the government. The removal of entry restrictions effectively removed the secondary market for taxi licences and with it the exorbitant cost of entry for new participants. The change signalled a removal of “discrimination against entrants” and so is now more akin to a contestable market.

In order to determine whether the taxi market in the post deregulation period represents an improvement in services to passengers, I undertook a study of waiting times for both taxis and passengers at the College Green rank in the city centre on Thursday 29th of January. The study was conducted over three periods during the day i.e. 9am-10am, 4pm-5pm and 11pm-1am. I will compare these results to those obtained from the 1998 Goodbody study (outlined above), to determine the level of improvement in the service since the removal of entry restrictions.

- *9am-10am:*

I considered this period to be a peak time given that it was a busy weekday morning and the level of congestion observable. During the period there were 57 pick-ups. I found that of these pick-ups, over half of passengers had no wait at all at the rank, while for those who did queue, the average wait for a taxi was only 3 minutes 20 seconds. The longest passenger wait was 9 minutes 20 seconds, but this was unrepresentative of the period as a whole.

For taxis, 41 had to wait at the rank for hire, the average wait being 2 minutes 9 seconds. In general, over the period I found that taxis were waiting on passengers rather than the other way around and that service was brisk and queues rare.

- *4pm-5pm*

Again, I expected this to be a busy period, though it was less busy than the morning period with 49 pick-ups. In this instance, no passengers had to wait for taxis. All taxis had to wait for hire at the rank, though these periods were generally short, the average wait being 3 minutes 21 seconds and the longest, 8 minutes 26 seconds. The average number of taxis at the rank was 3.75, the maximum being 6 at any one time.

- *11pm-1am*

This period was the busiest with 95 pick-ups in the first hour and 87 in the second hour. Again I found that customer demand was met effectively, as only 12% of passengers had to wait for a taxi. However, the average wait in this instance was very small, the average being 21 seconds and the longest, 35 seconds. The average wait for taxis was again small, as taxis waited for an average of 1 minute 46 seconds in the first hour and 1 minute 52 seconds in the second hour. The longest wait for a taxi was 12 minutes; however, only 3 taxis wait approached this length. Only 6% of taxis had a wait of longer than 5 minutes. I observed that at this time there was very little congestion and an abundance of taxis visible for hire, both at the ranks and on street.

From my own study and in comparison with the 1998 Goodbody report, I can conclude that things are indeed better for taxi users in 2004, c. 3 years after deregulation than when the taxi market was regulated. In that, deregulation has had a positive effect in terms of service to customers.

The 1998 Goodbody report indicated that there was a shortage of taxis in operation at the time, that lengthy wait times (in excess of 90 minutes) were common and that there was overall dissatisfaction among consumers re: taxi availability. The report concluded that:

“Restrictions on market entry should be avoided as regulatory authorities are unlikely to have sufficient foreknowledge as to provide the optimum supply of taxis. In the longer term, therefore, economic theory and experiences elsewhere support a policy of open entry in the taxi market”. (Faber, 1998)

On the basis of my own findings above, I suggest that deregulation has had a positive outcome. Many of the negative externalities associated with supply problems have been eliminated, such that taxis waiting at ranks is the standard, rather than the lengthy queues mentioned in the Goodbody report. In contrast to the 90 minutes wait times mentioned in the report, the longest wait time observed in the

study on the 29th of January was only 9 minutes 20 seconds, which was by no means representative of overall wait times as the majority of passengers had no wait at all. Thus, even from elementary comparisons it is possible to conclude that there has been a dramatic increase in the availability of taxis for consumers. There are no supply problems even at peak times and taxi travel has become a feasible transport option for a greater number of people.

In spite of the success of deregulation in this regard however, there remains a threat to the current system in terms of possible 'regulatory recapture'. One could suggest that with current supply in excess of 10,000 units, if entry is once again restricted, the externalities will not be as severe as those previously. However, given current growth trends, the problems posed by regulatory recapture are not insignificant. Such a move would also prove detrimental to efforts to reduce entry barriers in other transport sectors. Efforts must be made to ensure that lobby groups do not have the power to sway government policy. Recent examples of attempts at regulatory recapture may be observed in recent press releases. For Example, a recent article in the *Irish Independent* entitled *How Safe are Dublin Taximen*, in which, the vice-president of the National Taxi Drivers Union (NTDU) tries to draw attention to 'problems' caused by deregulation. Safety fears are also highlighted. TD Roisin Shorthall is quoted as saying that:

"Before deregulation, there was a fair degree of assurance that if taxi drivers had forked out up to €100,000 for a licence, they were highly unlikely to jeopardise their investment by carrying out any kind of assault. The very fact that the industry was so difficult to get into was a kind of guarantee of safety to passengers" (Irish Independent, 2004)

This kind of sentiment is misleading to taxi users, as this is not an adequate argument for regulation of entry, but rather for quality and safety standards for drivers and vehicles. A similar article from the *Sunday Independent* recently was headed *Rise In Attacks By Taxi-Drivers Leads To Calls For Checks*. In this article, Vinnie Jones of the NTDU claims: "even where applications for taxi licences have been refused, some applicants with dubious backgrounds have been successful in making challenges in the courts" (Sunday Independent, 2004). These types of scare tactics are, in my view another attempt at regulatory recapture and echo the sentiment expressed in the Taxi Forum release in 1998:

"Taxis with regulated fares and high cost of entry need to be protected from the hackney business where fares are not regulated and significantly lower costs of entry apply" (Dublin Taxi forum, 1998).

This release also suggested a points system for the awarding of licences and a phased increase in taxi licences up to 3,200 in 2002 (Ibid). It is obvious that this

system would have been wholly inadequate in dealing with supply problems of the time and is merely an attempt to maintain some kind of restraint on the number of operators with a view to maintaining the monopoly rents earned by the incumbents.

What is required is the type of policies advocated by the 1997 report: *The Dublin Taxi Market: Re-Regulate Or Stay Queuing?* This report highlights the need for free entry to the market to be accompanied with a strengthening of fare controls and safety standards. They indicate that safety fears and quality standards do not provide a case for regulation of entry:

“The only systematic problem that has accompanied entry deregulation is that quality standards have fallen as the market expands. However, this is a reason for improved quality standards rather than an argument against removing entry controls” (Fingleton et al, 1997).

It is imperative that this is the view taken and upheld by the government also. A possible source of concern in this regard is the appointment of an interim regulator in 2003, whose responsibilities include bringing stability to the industry and establishing lasting career opportunities for all those involved (Barrett, 2003). Although regulation is welcomed in the areas of fare and quality control etc., there are dangers in giving regulatory powers to one office in that this office provides an easy target for lobbyists leading to pressures, which could threaten the improvements brought about by liberalisation.

The breakdown of the current system could be harmful to policies aimed at increasing competition in other transport sectors (e.g. bus privatisation) for which the taxi model may provide a blueprint. For example, falling safety standards in the taxi market may be used as an argument against deregulation in other sectors.

Successes in this area invariably spread enthusiasm for the benefits of competition elsewhere, the deregulation of the city centre - Dublin Airport bus route being a case in point. TD Des O'Malley (2000) commented on the success: “deregulation should spread the benefits of competition through the country”

Conclusion:

There is ample evidence that the benefits of taxi market liberalisation have been substantial in terms of improving the availability and accessibility of taxis to consumers. The improvement of contestability has allowed the market to achieve more optimal outcomes. However, we must note that taxi liberalisation does not end with freedom of entry. To ensure the smooth running of the market, to eliminate the threat of regulatory recapture and to provide an exemplary model to liberalisation policies elsewhere, other reforms are also necessary. The Competition Authority presents this view in its 2002 report:

“More systematic regulatory reform is required if the taxi market is to function efficiently and deliver maximum benefit to consumers, the taxi industry and the overall economy...otherwise there is a risk that the deregulation of entry to the taxi market in isolation, could undermine support for regulatory reform more generally” (Competition Authority, 2002).

It is evident that, in respect to deregulation and privatisation that the Irish Government lags behind some of its international counterparts (OECD, 2001). So it is imperative that the taxi liberalisation policy does not provide arguments against liberalisation in other sectors of the economy. In this way there will be no impediment to the benefits of competition in the economy and the government can switch its attention away from market intervention towards the provision of pure public goods, which is invariably the socially optimal outcome (Barrett, 2003).

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