VACC's submission to the Essential Services Commission's accident towing fees review 2021

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Contents

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Introduction

The Victorian Automotive Chamber of Commerce ('VACC') is Victoria's peak automotive industry association, representing the interests of more than 5,000 members in over 20 retail automotive sectors that employ over 50,000 Victorians.

VACC welcomes the opportunity to provide the ESC with this submission in response to the ESC's *Accident towing fees review 2021 Consultation paper* ('the Consultation Paper'). VACC's submission covers three key areas in detail before providing an itemised response to the ESC's list of stakeholder questions. The key areas covered are:

- the background to the factors affecting the industry that VACC considers are relevant for the ESC's recommendation under section 212A of the *Accident Towing Services Act 2007* (Vic) ('the Act')
- the need for a cost-of-service methodology, with a benchmarking approach not appropriate
- the need to set a productivity adjustment figure of negative 0.5 per cent, as the default figure of 0.5 per cent a year is not appropriate.

Included as an appendix to this submission is a cost-of-service model approach prepared by Deloitte Access Economics. Deloitte Access Economics has also assisted VACC with developing this submission.

Background on the current state of the industry

The accident towing industry has a strong desire to enhance safety outcomes and be recognised as a genuine essential service

The accident towing industry is a key part of Victoria's accident response system. Its work contributes to a safer road network across the Melbourne controlled area and beyond. Timely removal of damaged vehicles also has a considerable economic impact by reducing congestion.

The industry is committed to the purpose of the Act, namely "to promote the safe, efficient and timely provision of accident towing services and other related services". The industry's safety commitment is mirrored by the objectives of the Victorian Government's *Victorian Road Safety Strategy 2021-2030*[i], to increase safety for those using the road for work or at work, and to embed a culture of road safety within the Victorian community.

Accident tow trucks play an essential role in responding to accidents, and sometimes arrive at the accident scene in advance of other responders. As such, the tow truck industry is seeking, in the long term, to move towards recognition as a genuine essential service including enhanced safety measures such as speed restrictions around operating vehicles.

The industry is facing significant external pressures that directly affect costs

The accident towing industry in the Melbourne controlled area is working to respond to changing circumstances. To help it do so, and to ensure that the industry remains competitive and well-run, we need an effective regulatory framework and fairly set prices. A range of external factors has affected the industry's operation in recent years. These effects have occurred since 2009, the last time the ESC reviewed the appropriateness of the accident towing fees on a cost-of-service basis, including since 2018, when the fees were last reviewed on a benchmarking basis.

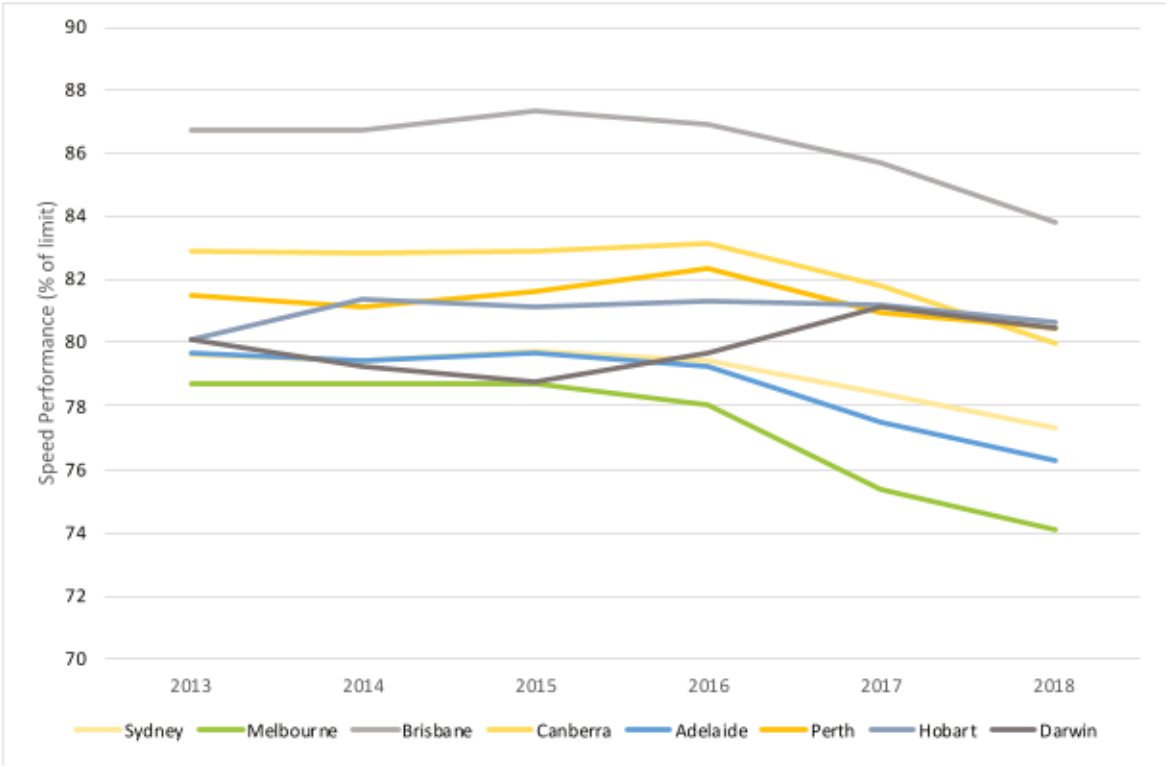
In summary, traffic congestion has increased across Melbourne's road network (see Figure 1). This increasing congestion has increased the amount of time taken to respond to each call-out. In addition, the monthly number of allocations has been stagnant since 2018 (see Figure 3), reducing revenue for the accident towing industry. Further, new vehicle technologies have increased significantly, and will continue to increase, the complexity (and time and cost) of call-outs. Together, these external pressures have increased the number of truck hours that the accident towing industry has had to support each year with lower revenue, in an environment of rising costs (such as labour and vehicle running costs) and high regulation (such as safety and licensing).

Congestion increasing

Traffic congestion has increased, with Melbourne's average speeds as a proportion of the speed limit decreasing by nearly 5 per cent between 2013 and 2018 (see Figure 1). Melbourne's speeds as a proportion of the speed limit have dropped by the most of all capital cities and are the lowest of all capital cities. In addition, speed limits in Melbourne have generally decreased in recent years, particularly in and around the CBD.[ii] This has created additional pressure on tow truck drivers, who are required to attend accident scenes within 30 minutes of being given an authorisation to attend.

Putting aside the temporary impacts of COVID-19, this pressure is only likely to increase as congestion increases further in the future. The latest Australian State of the Environment Report in 2016 noted that, under currently expected patterns of metropolitan population growth, a steady increase in aggregate urban traffic is likely in the next 15 years, with total vehicle-kilometres travelled forecast to increase by around two per cent per year to 2030.[iii]

Figure 1: Average speeds as a proportion of the speed limit (%)



Source: Australian Automobile Association

Even as congestion has increased overall, the accident towing industry has contributed to reducing congestion bottlenecks around accident scenes. Infrastructure Australia noted in 2016 that without action, the cost of congestion in Australia's major cities, including increased travel times and lost productivity, was set to rise from nearly $14 billion in 2011 to over $53 billion in 2031.[iv] The Bureau of Infrastructure, Transport and Regional Economics splits out the "avoidable" cost of congestion, highlighting that in 2014-15, congestion was estimated to have caused $16.5 billion in such costs, including approximately $6 billion in private time costs, $8 billion in business time costs, $1.5 billion in extra vehicle operating costs, and $1 billion in additional air pollution costs.[v] Every time a tow truck clears away an accident vehicle that is blocking traffic, congestion and its associated costs are reduced.

Accident tow truck allocations declining since 2018

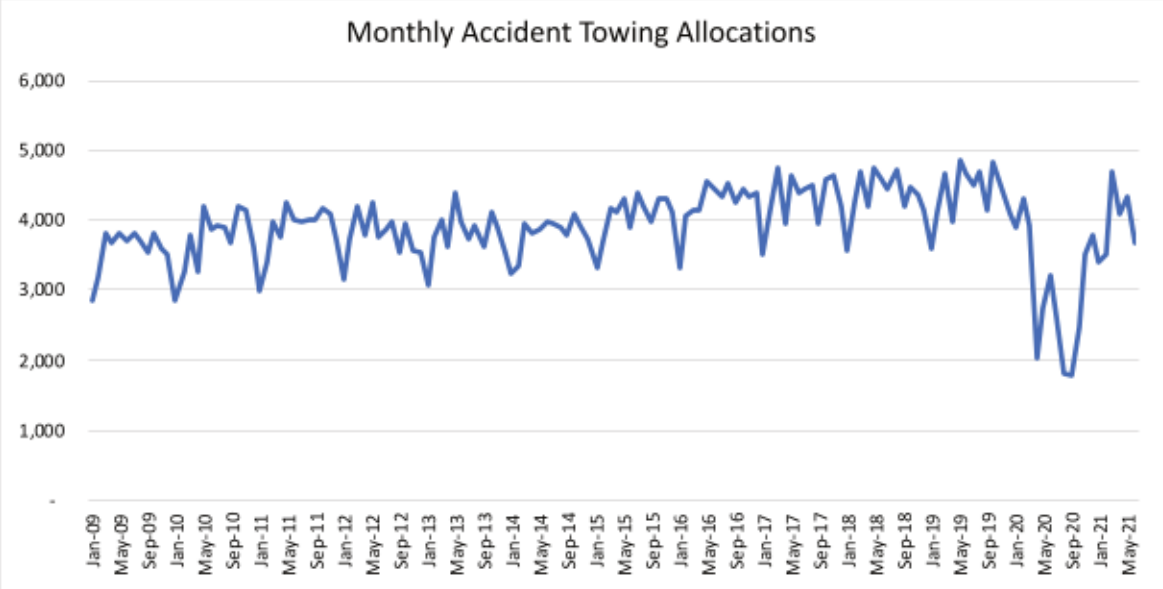
From 2009 to 2019, the number of tow truck allocations to accident scenes trended gradually upwards over time (see Figure 2). This required the accident towing industry to support more truck hours each year. As part of the ESC's 2018 review, its consultants, Advisian, commented that "we expect an ongoing future source of potential productivity gains will be through

continued increasing numbers of accident utilisations in the Melbourne Controlled Area, enabling opportunities for improved tow truck utilisation. The historically increasing number of accident allocations is likely to be closely linked with traffic growth, which is forecast to continue as Melbourne's population and travel demand grows."[vi]

However, since 2019, there has been essentially no growth in accident towing allocations pre-COVID-19, and then a steep decline during the extended lockdown periods in Melbourne (see Figure 3). While the industry is pleased that fewer accidents have occurred, a consequence of fewer accident towing allocations is a higher cost per tow for the accident towing industry.

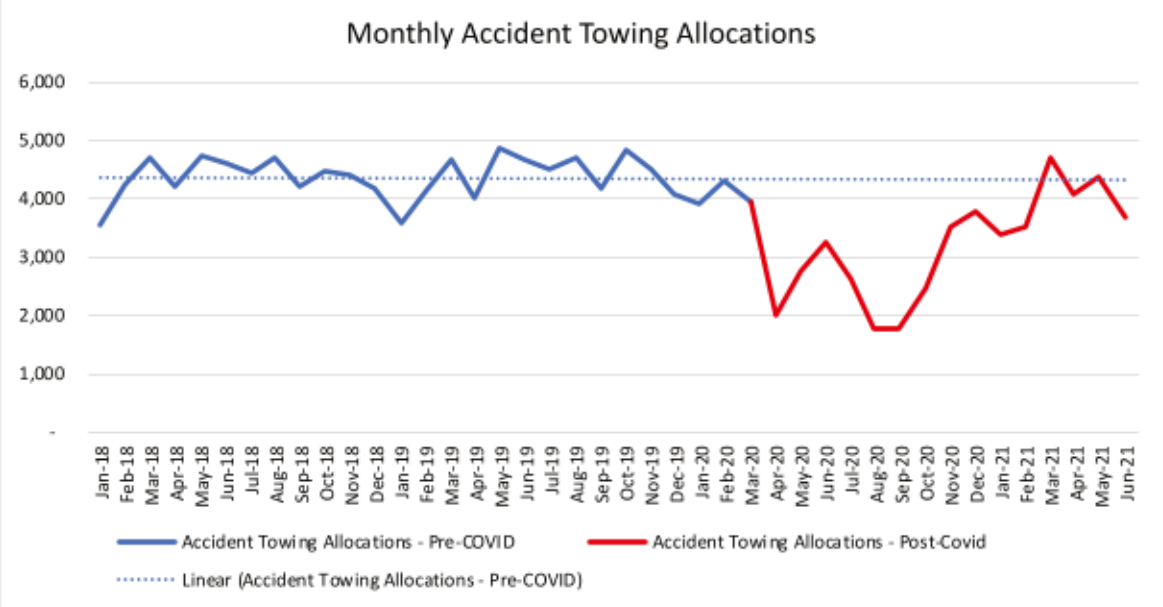
Just as significant is the ever-increasing level of vehicle crash avoidance technology in new cars, including radar and lidar systems. These and other vehicle automation systems will significantly reduce the number and impact of vehicle collisions in the years ahead. It is likely that these technologies, along with reduced vehicle travel speeds, are already reducing the number of vehicle collisions and accidents in Victoria.

Figure 2: VicRoads Accident Tow Truck Allocations January 2009 – June 2021



Source: VicRoads

Figure 3: VicRoads Accident Tow Truck Allocations January 2018 – June 2021



Source: VicRoads; Deloitte Access Economics

In terms of likely future trends in accident towing allocations, governments at federal, state and local levels have adopted strategies to continue to reduce the number of accidents.[vii] VACC welcomes many of these policy developments, but notes that a by-product of fewer accidents in the future would be lower allocations for accident towing operators. While the accident towing industry is continuing to seek ways to reduce costs, factors such as rising real wages and fixed costs such as rent make it extremely challenging to reduce costs to match the reduction in revenue.

Labour costs rising

Labour costs account for a significant part of the overall costs for the towing industry. Labour costs for the towing industry have risen by approximately 35 per cent since the ESC's last cost-of-service review in 2009. These costs have risen by approximately 6 per cent since the last benchmarking review in 2018 (see Table 1).

Table 1: Increase in Total Hourly Rates of Pay Excluding Bonus as at March 2021

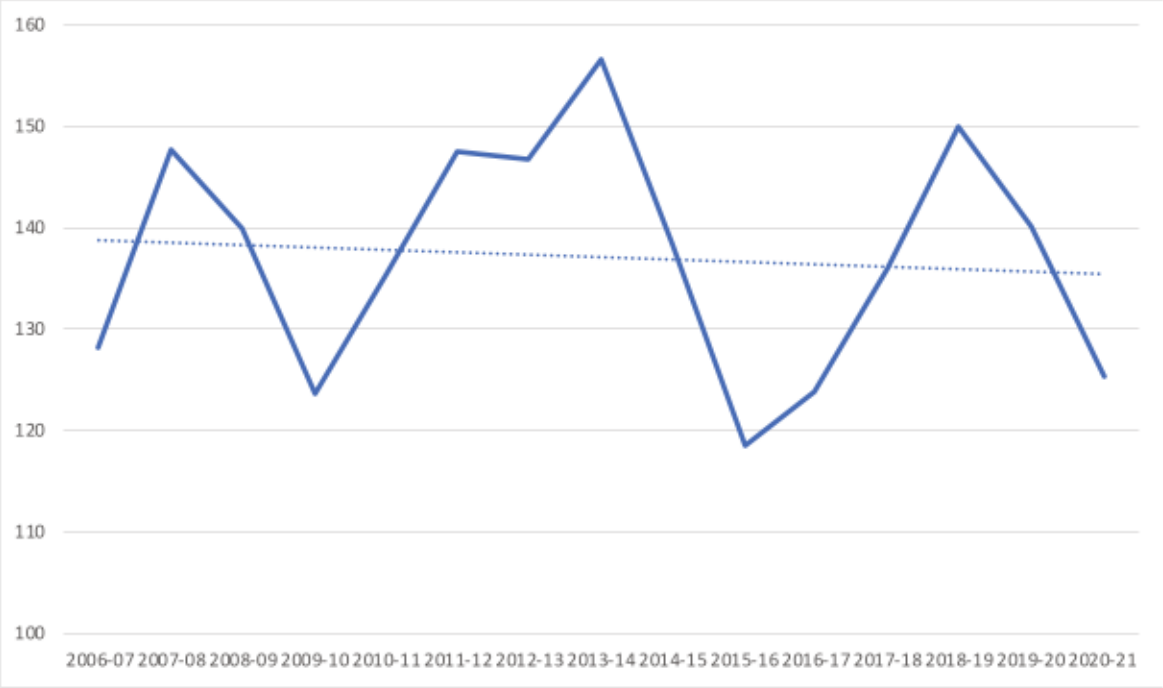
Geography	Australia	Australia	Victoria	Australia	Australia
Sector	Public & Private	Private	Public & Private	Public & Private	Private
Industry	All	All	All	Transport, Postal and Warehousing	Transport, Postal and Warehousing
% Growth from March 2018	6.16%	6.04%	6.83%	6.07%	6.10%
% Growth from March 2009	35.42%	34.43%	36.92%	35.12%	34.49%

Source: ABS

Fuel costs volatile, set to increase

Fuel costs have been highly volatile with a very slight downward trend in diesel prices since 2006-07. Figure 4 shows that this long-term downward trend is largely due to low average diesel prices in the last few years, a product of the COVID-19 downturn and subsequent intense price competition among oil producers. Diesel prices have, however, steadily risen from the start of 2021 and are up by 17.7% in the period to 11th July 2021.

Figure 4: Average Diesel Pump Price (cents) by Financial Year



Source: Australian Institute of Petroleum

Lease costs rising

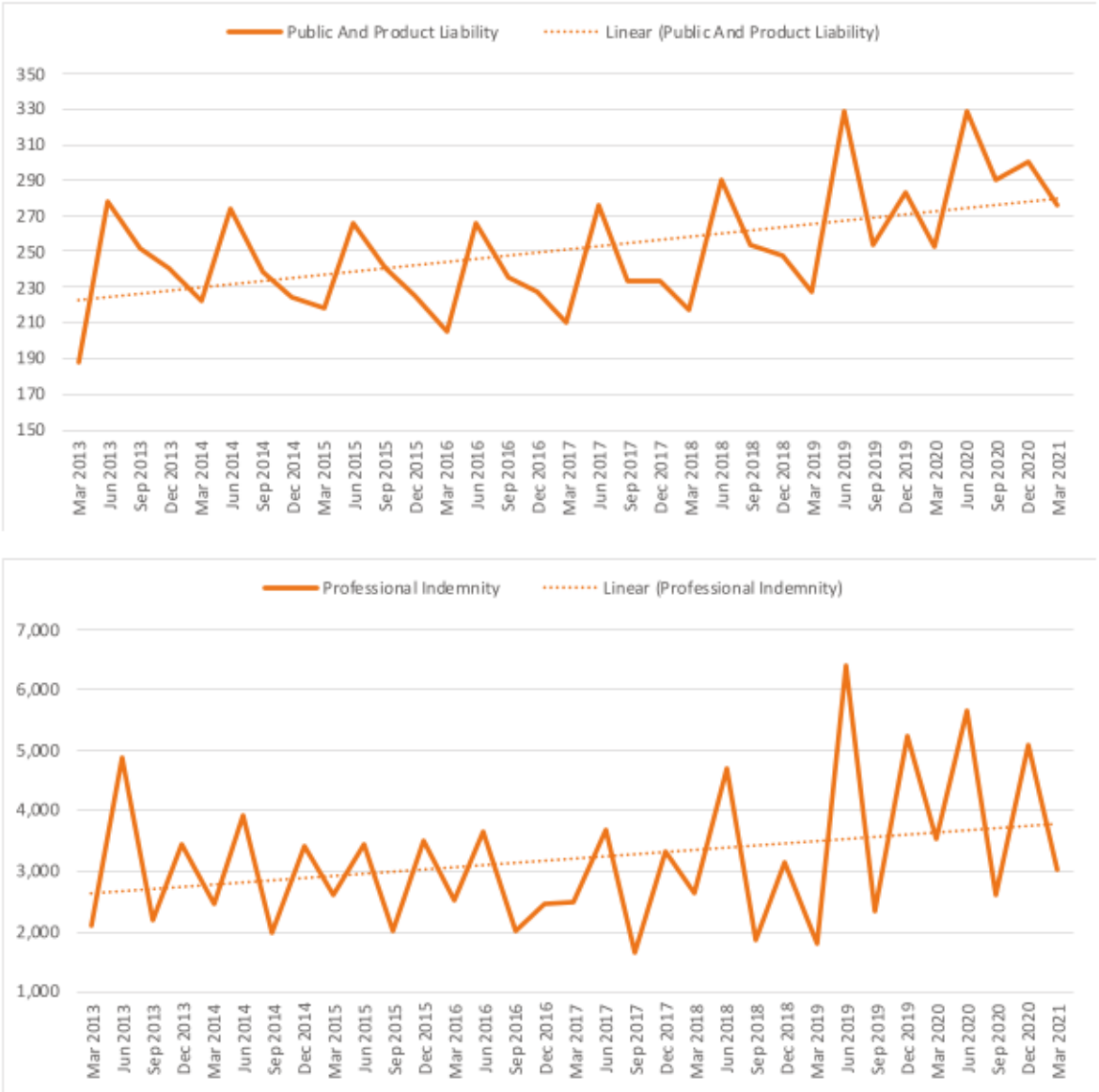
In order to meet customer expectations and regulatory standards, tow trucks need to be located close to areas where accidents occur. This requires depots in high traffic, high-demand real estate areas.

In 2014, a survey of industrial zones across the areas where accident towing depots are located indicated an average lease cost of $90 per square metre (including outgoings). A subsequent survey, cited in VACC's submission to ESC's 2018 review, indicated lease costs of $120 per sq m for inner Melbourne and $100 per sq m for outer Melbourne.[viii] In the first quarter of 2021, Melbourne city fringe industrial rents were $107.50 to $202.50 per square metre (including rental net face and outgoings), while outer eastern areas (such as Mulgrave, Clayton, Rowville, Scoresby, Notting Hill and Knoxfield) were $93 to $120 per sq m (including rental net face and outgoings).[ix] Further, commercial and industrial property sales in metropolitan Melbourne rose 10.5 per cent between 2019 and 2020, indicating an increase since the last review.[x]

Insurance costs rising

APRA data, below in Figure 5, shows the quarter-by-quarter increase in premium ($) per risk associated with Public and Product Liability and Professional Indemnity Insurance classes in Australia rising by 47% and 43% respectively over the period March 2013 – March 2021.

Figure 5: Insurance Cost Trends: Average premium ($) per risk in Australia by Insurance type



Source: Australian Prudential Regulation Authority (APRA)

Regulatory obligations increasing

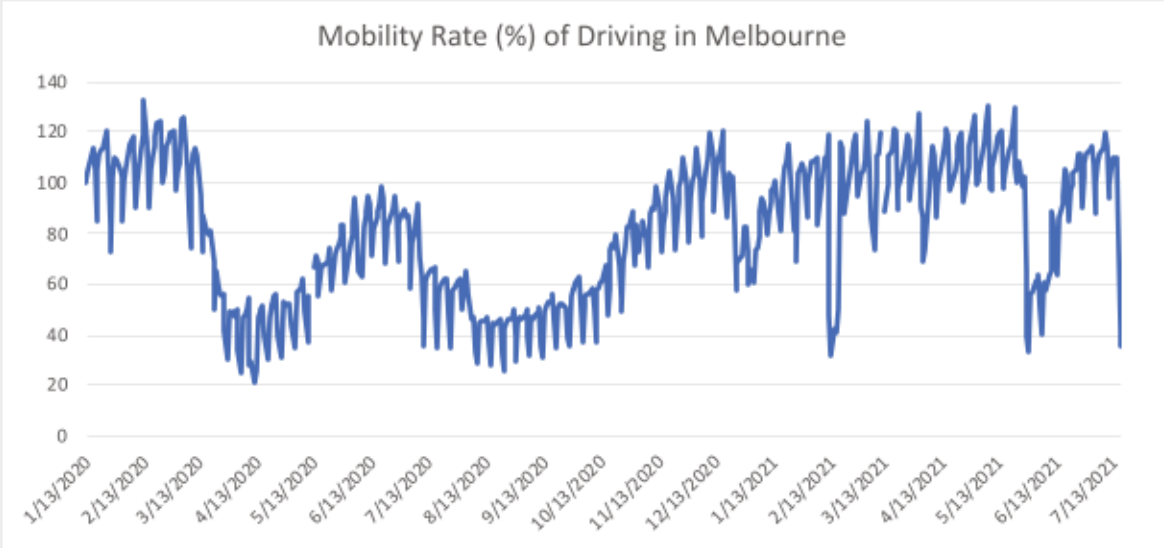
The Accident Towing Services Regulations 2019 (Vic) began operation on 14 December 2019, imposing renewed regulations on the accident towing industry covering matters such as accreditation, qualifications, training, record keeping, safety, vehicle specifications and operations. Rising obligations from these new regulations and liabilities in the industry present increased risks to a towing business where the external environment is not in the control of the operator. This important matter has been raised with the Victorian Government.

COVID-19 led to a reduction in demand for our services

Overall, the COVID-19 pandemic has had a significant negative effect on the accident towing industry.

Mobility data, Victorian SCATS data and petrol sales all suggest fewer cars on Melbourne's roads during the extended periods of lockdown in 2020 and 2021.[xi] From baseline mobility data taken in January 2020, Figure 6 shows a significant decrease in people driving throughout the COVID-19 pandemic, particularly between March 2020 and November 2020.

Figure 6: Driving Mobility Rate throughout COVID-19 Pandemic

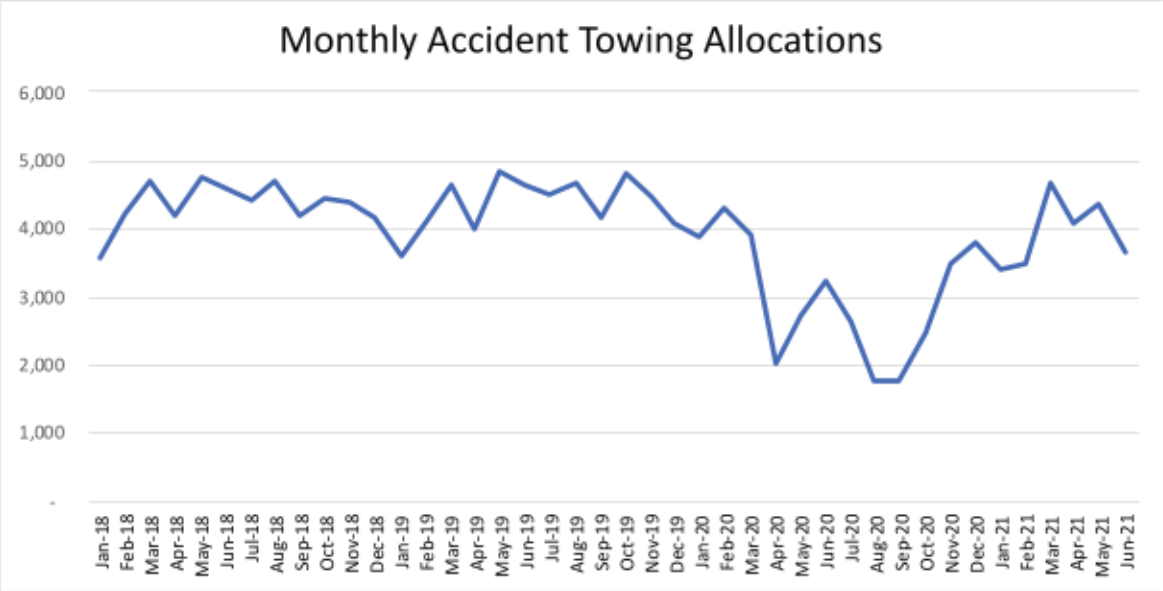


Source: Apple Mobility Trends

As an example of how changes in traffic affected the road network, the Monash Freeway experienced a 28 per cent reduction in vehicles and a congestion reduction of between 88 and 95 per cent for weekday peak periods towards the end of March 2020.[xii]

This reduction in cars on the road led to far fewer accidents. Figure 7 shows a significant decrease in accident allocations during the COVID-19 pandemic extended lockdowns. Fewer accidents during these lockdowns, while clearly beneficial for the community, resulted in decreased revenue from accident towing fees for the industry. VACC notes that 81 percent of towing operators utilised JobKeeper in Victoria.[xiii]

Figure 7: VicRoads Accident Tow Truck Allocations January 2018 – June 2021



Source: VicRoads

The reduction in towing allocations is a critical challenge for the industry as, even though the number of call outs decreased, fixed costs remained largely unchanged. To meet the regulatory requirement to attend an accident scene within 30 minutes, accident tow truck operators need to have a tow truck, driver, office, receptionist and storage space available at all times.

New technologies are working to reduce crashes and increase complexity of service

In the short term, the Victorian car fleet is changing in terms of the level of safety available and, over the longer term, will see significant changes in technology – including electrification and greater vehicle autonomy.

VACC strongly supports the Victorian Government's work to remove older vehicles with fewer effective safety features from Victorian roads.[xiv] This process is likely to significantly reduce the number of crashes over time. While this is clearly a benefit to the community and one that the accident towing industry welcomes, this will have an impact on the industry, as fewer accidents means fewer call-outs.

In terms of new vehicle sales by fuel type, petrol and diesel vehicle sales have declined marginally since at least 2018. VACC modelling predicts limited growth for these vehicles from 2021 to 2023. In their place, recent strong growth in newer technology hybrid vehicle sales is expected to continue, with at least a doubling of 2020 sales forecast for 2023. The strongest sales growth, off a low base, is expected to be for new technology electric and plug-in-hybrid vehicles.[xv] Vehicles that incorporate batteries are often heavier and pose challenging fire risks when compared with traditional internal combustion engine vehicles.

New cars come with new technology, such as electric batteries or advanced braking systems, that can increase the complexity of accident towing. For example, after an accident, an advanced braking system may lock and require expert advice to be sought to enable the car to be towed. Additional technologies likely to enter Australia in the medium term, such as hydrogen fuel cell vehicles and Level 3 and 4 autonomous vehicles, will further increase the complexity of post-accident care.[xvi] This is likely to further increase the time taken for each call, as well as require further upskilling of employees, adding to industry costs. Tooling and resourcing required for the treatment of electric, fuel cell or hydrogen vehicles at an accident scene need to be factored into the overall costs to an accident towing operator.

Responses to key topics

This section provides a response to the ESC's question for consultation as to whether existing regulated fees are appropriate. It focuses on the overall methodology and the productivity adjustment figure. VACC sees these issues as the two key components of the upcoming recommendation by the ESC.

Methodology

VACC considers that the current level of charges is not appropriate for maintaining a safe, efficient and timely accident towing service.

As costs have increased in the accident towing industry, accident towing operators have adopted efficiency measures to enable their businesses to survive. However, operators have regulatory obligations that they must meet, including work, health and safety obligations, and obligations to attend accident scenes within 30 minutes. VACC is concerned that the current regulated fee levels have the potential to place ongoing pressure on the industry's ability to deliver on its safety and timeliness objectives. VACC is concerned that, if the regulated fees are set too low, it could force out operators who comply with regulations, as has occurred in the waste industry.

VACC considers that it is an appropriate time to undertake a holistic pricing review to ensure the current and future sustainability of a towing industry that can provide safe, efficient and timely service for Melbourne's motorists. COVID-19 has caused significant disruption to the community. The Victorian Government has a new ten-year road safety strategy. It is appropriate for the ESC to undertake a review of costs to ensure that the accident towing industry is on a sustainable basis into the future.

VACC strongly argues that cost of service should be the basis for the fee review, as significant time has passed with benchmarking alone being relied upon. A benchmarking approach essentially operates to verify that historical cost-of-service approaches are still providing relevant prices. Over time, benchmarking will likely become less reliable as the original pricing basis becomes more out of date and less reflective of current industry cost structures. As an example, the ESC last carried out a cost-of-service review for accident towing fees in 2009. Labour costs alone have increased by approximately 35 per cent since 2009 (see Table 1).

VACC considers further that benchmarking is not appropriate in the current circumstances due to the difficulty of making comparisons between jurisdictions. Previous benchmarking by the ESC has noted the presence of different levels and types of regulation between jurisdictions as well as the role that different cost bases, congestion and service standards play in making this type of assessment. Different service standards and different levels of congestion also play a role. For example, while accident tows are allocated in the Melbourne controlled area, in Sydney a towing authorisation can be sought at the scene of the accident. In relation to congestion, as noted earlier in this submission, Melbourne's traffic speeds as a proportion of the speed limit have dropped by the most of all capital cities and are the lowest of all capital cities (see Figure 1). In practice, difficulties in comparison have meant that the ESC has relied on a hybrid approach where benchmarks are passed through a basic cost-of-service model to provide realistic points of comparison.

Further, in many cases the ESC is benchmarking regulated prices in Victoria against regulated prices elsewhere in Australia. The ongoing reliance on benchmarking risks creating a feedback loop of regulatory decisions without being brought back to a contemporary evidence base.

The industry strongly advocates for the use of a cost-of-service methodology. VACC acknowledges the ESC's 2018 consideration of both a cost-of-service approach and a benchmarking approach, including "the difficulty and time required to obtain the required cost information to undertake a cost of service approach".[xvii] Consequently, the industry now proposes a significantly simplified cost-of-service model approach which is set out in the appendix to this submission. This cost-of-

service model approach has been developed by Deloitte Access Economics to balance the need to build a genuine evidence base on costs with the risks around data availability and reliability.

The industry would support this, or a similar method being applied and would be happy to provide information to support its application. VACC offered to assist in the development of a cost methodology following the ESC's 2018 review.[xviii] VACC renews its offer to draw upon its resources and provide the ESC with access to its members, if needed. VACC would also welcome the opportunity to work with insurers, VicRoads and other stakeholders to determine the final cost-of-service methodology to apply.

Given the changes in the costs of inputs, the number of crashes and vehicle technology, VACC sees the need for a cost-of-service approach to be developed at some point and now is an ideal time.

Productivity adjustment figure

VACC submits that the default 0.5 per cent productivity adjustment figure is not appropriate and should not be applied. VACC requests that the ESC exercises its power under section 212A(1)(c) of the Act to recommend a different figure.

The productivity adjustment figure represents an amount by which the accident towing industry is expected to outperform productivity changes in the broader Melbourne transport industry. Achieving material annual productivity gains is not currently possible in the accident towing industry in the Melbourne controlled area and is certainly not possible year after year.

VACC submits that it has been very difficult for the accident towing industry, due to its structure and function, to improve its productivity relative to the broader Melbourne transport industry. Indeed, the following features of its industry are likely to have meant it has achieved lower productivity improvements than the broader transport industry:

- the volume and allocation of output (accident towing) is not controlled by the industry
- capital productivity is hampered by tight regulation that prevents flexible use of new or additional equipment and implementation of new technologies, hindering operators' abilities to control input quantities
- increased congestion is likely to be contributing to cost increases
- rising operational and compliance costs.

On the latter point above, it is clear that, after accounting for the limitations on productivity improvements discussed below, a key impact on productivity in the industry is congestion, a factor outside the industry's control. As discussed in the "Background on the current state of the industry" section above, congestion is rapidly worsening in Melbourne.

Volume of output

A primary method through which increased productivity is achieved in the economy and the transport sector is by creating more output from the same inputs. In the case of the accident towing industry the level of output of any one operator is determined by the overall number of accidents and, in the Melbourne controlled area, by the centralised allocation mechanism. As a result, there can be a lot of downtime, and operators do not have any capacity to materially increase their level of output and enhance their productivity.

Capital productivity

Capital productivity is often achieved through using new technology or increasing the utilisation of existing capital.

In terms of increasing utilisation, this is entirely determined by the frequency of tows being allocated to each truck. The allocation of tows is determined by the number of accident towing licences that each truck has. In practice, the accident towing industry has a largely fixed number

of licences, determined by legislation. The issuing of new tow truck licences is subject to a public interest test under the Act, and there have been no new licences issued since the 1980s other than for CityLink and Peninsula Link, largely due to declining numbers of road accidents.[xix]

The ability to make better use of technology is also limited due to operational regulation by VicRoads. For example, one area where capital productivity could be increased is by towing multiple vehicles with a single truck. However, the Accident Towing Services Regulations 2019 (Vic) prevent an accident tow truck driver from towing more than one accident-damaged car in the Melbourne controlled area.

Labour and other input productivity

The accident towing industry is highly regulated with requirements to achieve arrival times of 30 minutes or less. This creates the need to maintain a high level of stability in the input requirements in terms of truck operators. Requirements around ensuring specified depots are open and staffed between 8 am and 5 pm Monday to Friday (excl. public holidays) lock in some additional labour costs. This means that the industry cannot significantly adjust the quantity of labour inputs below a certain level.

On the cost side, the consumable cost base is largely out of the operators' control. Fuel, repairs, licence fees, registration, land rates/lease costs etc. are all determined in highly competitive markets or set by government.

Taken together, with little control over the quantity of labour and non-labour input and little to no control over the cost of these inputs, the industry has very limited opportunities to pursue ongoing productivity gains by reducing the total costs of labour and other inputs.

Relevant productivity adjustment factor considerations

From a technical perspective, VACC does not agree with the ESC's 2018 analysis of the productivity adjustment figure. Analysis of the potential range of productivity adjustment figures that could be calculated for the accident towing industry is provided in the appendix by Deloitte Access Economics. VACC supports Deloitte's key arguments, namely:

- reiterating the point raised by Advisian in the 2018 review that the Transport CPI already incorporates industry-wide productivity improvements, and
- that the evidence presented by Advisian in the 2018 review indicates that different measures of productivity in the industry could range from significantly negative to large positive values. This indicates that there is no compelling evidence for any productivity improvement in the accident towing industry.

VACC also notes that, while the ESC has scope under other legislation to apply efficiency factors, it has elected not to do so in recent years, for example, when advising the Minister for Local Government in relation to the average rate cap for councils under the Local Government Act 1989 (Vic).

As a result of the difficulty in achieving ongoing productivity improvements, in an environment of higher traffic congestion and essentially no growth in the number of accident tows per truck since 2018 (as per Figure 3), VACC strongly recommends that the ESC exercise its power under section 212A(1)(c) of the Act to recommend a productivity adjustment figure of minus 0.5 per cent (i.e. applied under section 212H of the Act as CPI plus 0.5 per cent).

VACC considers this to be a modest proposal, given that analysis presented by Deloitte Access Economics in the appendix to this submission indicates that productivity in the towing industry has been stagnant over the medium term and has declined significantly under COVID-19 conditions. In particular, the ABS estimates that multifactor productivity for the Transport, Postal and Warehousing division has declined by around 1.7% a year since 2017-18.

VACC considers this methodology would most accurately reflect realistic productivity improvements possible within the confines of the highly regulated accident towing industry relative to the broader Melbourne transport sector. This would also ensure the promotion of safe, efficient and timely provision of accident towing services and other related services. Ongoing and unachievable productivity improvements will, over time, work to diminish safety and timeliness.

Response to questions

While the key issues that VACC wishes to respond to are discussed above, this section sets out VACC's responses to the stakeholder questions set out in Appendix C of the Consultation Paper.

Have there been any significant changes in the industry since our last review?

1. Have there been any significant changes in the accident towing industry since 2018?

Please refer to "Background on the current state of the industry."

2. Have the costs of accident towing operators changed since 2018? Can any significant cost changes be supported with material illustrating these changes?

Please refer to "Background on the current state of the industry."

3. How has the coronavirus pandemic affected your participation in the accident towing industry, if at all? If so, can you provide data to illustrate these impacts?

Please refer to "Background on the current state of the industry."

4. Have there been any significant changes related to the coronavirus pandemic or otherwise, that relate to other industries integrated with accident towing, such as trade towing or smash repairs?

VACC does not consider that these other industries are relevant for the purpose of the current review.

Should we recommend any changes to fees?

5. Are the current accident towing and storage fees appropriate? If not, do you consider they should increase or decrease? Why?

Accident towing services are a critically important part of accident response services in Victoria. The industry needs to be put on a sustainable basis for the future. In this context, VACC considers that the current accident towing and storage fees are not appropriate. VACC considers that all fees should be reviewed on a cost-of-service basis. The cost of providing the services has not been reviewed by the ESC in detail since 2009.

VACC considers that it is likely that a full cost-of-service review would indicate that the fees should be increased but VACC would support an evidence-based finding.

6. What type of methodology should we use to assess fees for the Accident towing fees review 2021?

VACC considers that all fees should be reviewed on a cost-of-service basis. VACC acknowledges the ESC's 2018 consideration of both a cost-of-service approach and a benchmarking approach, including "the difficulty and time required to obtain the required cost information to undertake a cost of service approach". Consequently, we propose a simplified cost-of-service model that could be easily implemented. VACC would be happy to work with the ESC and insurers to agree and implement such a model.

7. Do you agree with the benchmarks we previously used for the Accident towing fees review 2018? If not, what benchmarks would be appropriate?

No, as outlined above in our submission, VACC considers that a benchmarking approach is not appropriate. A cost-of-service approach would be appropriate.

Should we recommend changes to the productivity adjustment factor?

8. To what extent have accident towing businesses been able to reduce costs and improve their overall efficiency since our last review? What factors may have contributed to accident towing businesses' ability to reduce costs and improve efficiency?

As outlined above in our submission, VACC considers that, due to the structure and function of the accident towing industry, it has not been able to reduce costs and improve overall efficiency above and beyond the general transport industry since the ESC's 2018 review.

Factors that may have contributed to accident towing businesses' inability to enhance productivity include:

- the volume and allocation of output (accident towing) is not controlled by the industry
- capital productivity is hampered by tight regulation that prevent flexible use of new or additional equipment and implementation of new technologies
- input costs are generally beyond the control of the industry.

9. How has the coronavirus pandemic affected accident towing businesses productivity performance, if at all? If so, can you provide examples (such as a change in work practices) to demonstrate the impacts?

COVID-19 led to a significant reduction in the number of crashes during the extended lockdown periods while not affecting the industry's fixed costs. As a result it has significantly reduced the industry's productivity.

Please refer to "Background on the current state of the industry" for more details.

10. What productivity measures should we use to assess accident towing industry productivity?

As outlined above in our submission, VACC considers that a productivity adjustment of CPI plus 0.5 per cent is appropriate (i.e. a productivity adjustment figure of minus 0.5 per cent, rather than the default productivity adjustment figure of 0.5 per cent).

Should any unregulated services have a set fee?

11. Should fees for basic salvage services be regulated? If so, what is an appropriate regulated price for basic salvage services? What factors should we take into consideration to set fees?

Basic salvage services have a highly diverse range of requirements that do not lend themselves to either benchmarking or development of a cost-of-service model. As a result, VACC submits that fees for basic salvage services should continue to be unregulated.

12. Are the fees for basic salvage services transparent and reasonable? If not, how might this be rectified?

The VACC considers that the fees for basic salvage services are transparent and reasonable. The regulatory requirement for photographs, together with the requirement in section 212I of the Act that salvage charges are required to be reasonable, is providing ample protection against excessive charging.

13. To what extent, have the Accident Towing Services Regulations that relate to transparency, such as photographs been enforced?

VACC considers that the regulatory requirement to take photographs of each salvage operation provides the owner/insurer with the necessary evidence of the scale of the salvage work, and the likely time involved.

14. Are there any unregulated storage services that should be subject to a regulated price?

The VACC is not aware of any unregulated storage services that should be subject to a regulated price.

References

[i] *Victorian Road Safety Strategy 2021-2030*; link available

[ii] City of Melbourne, *City Speed Limits*; link available

[iii] Australia State of the Environment Increased traffic Built environment (2016); link available

[iv] Infrastructure Australia, *Australian Infrastructure Plan 2016*, p 48; link available

[v] Bureau of Infrastructure, Transport and Regional Economics, *Traffic and congestion cost trends for Australian capital cities*; link available

[vi] Advisian, *Accident towing fees in the Melbourne Controlled Area – Fee benchmarking and productivity review* (June 2018), p 36; link available

[vii] *National Road Safety Strategy 2021-30* – link available; *Victorian Road Safety Strategy 2021-2030* – link available; *City of Melbourne Transport Strategy 2030* – link available

[viii] *VACC submission Review of accident towing and storage fees 2018 Essential Services Commission*, May 2018

[ix] *Savills Research – Q1 2021 Quarter Time National Industrial*; link available

[x] *A Guide to Property Values – Annual analysis of property sales data from Valuer-General Victoria January – December 2020*, Table 3, p 6; link available

[xi] Australian Road Research Board, *Impact of COVID-19 on road crashes in Australia* (Oct 2020); link available

[xii] Australian Road Research Board, *Data sheds new light on COVID-19 effects* (Mar 2020), figures 3 and 4; link available

[xiii] Motor Traders Association of Australia, *Directions in Australia's Automotive Industry – An Industry Report 2021*; Link Available

[xiv] Transport Accident Commission, *Victorian Road Safety Strategy 2021-2030*; link available

[xv] VACC, *Directions in Australia's Automotive Industry – An Industry Report*, 2021, pp 54-55; link available

[xvi] VACC, *Directions in Australia's Automotive Industry – An Industry Report*, 2021, pp 62-64; link available

[xvii] Essential Services Commission, *Review of accident towing and storage fees – Final report* (Dec 2018), p 28; link available

[xviii] Essential Services Commission, *Review of accident towing and storage fees – Final report* (Dec 2018), p 8; link available

[xix] Accident Towing Services Regulations 2019 Regulatory Impact Statement, p 7; link available

[xx] Essential Services Commission, *Review of accident towing and storage fees – Final report* (Dec 2018), p 28; link available.

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Accident towing fees – cost of service and productivity

Victorian Automotive Chamber of Commerce

Deloitte Access Economics

Contents

1 Cost-of-service methodology

1.1 Principles of this cost-of-service methodology

A cost-of-service approach to assessing the appropriateness of accident towing services fees requires a review of the existing fees based on the estimated costs of providing those services.

The cost-of-service approach set out in this report is an initial definition of how a simplified cost of service model could be implemented and is intended to:

- ensure that the regulated pricing reflects the costs of providing a safe, efficient and timely regulated accident towing service
- ensure that no economic cross-subsidy occurs between regulated and unregulated portions of towing businesses
- minimise the data gathering requirements and cost for industry and the ESC
- enable constructive discussions between stakeholders on appropriate cost inputs
- enable ongoing productivity improvements to be reflected directly in input cost assumptions, and
- align with previous approaches used or proposed for adjusting benchmarking and reviewing storage costs.

1.2 Summary of methodology

This methodology seeks to establish a cost of service for a representative accident towing licence, accounting for the potential of inputs to be used in non-regulated activities. It is similar to cost build-up approaches used in other regulated industries such as electricity, water, internet and taxi services.

It is also similar to the analysis of efficient costs approach used by the NSW Independent Pricing and Regulatory Tribunal ('IPART') as part of its 2014 review of tow truck fees and licensing in NSW. Note, though, that this methodology is focused on the regulated accident towing service specifically and, unlike IPART, does not include detailed data on finances or benchmarking with unregulated towing services.[1]

If implemented using high quality information, this approach would ensure that pricing should recover costs that are between the stand-alone and incremental cost of providing regulatory services. It splits the total cost of service between the expected number of towing allocations to determine the price for each component of the towing service, taking into account how costs should be recovered from both fixed and variable components.

[1] IPART, *Review of tow truck fees and licensing in NSW: Transport – Final Report*, December 2014, p 37; link available

1.3 Cost build up approach

The methodology seeks to calculate the annual costs of providing the regulated service for a business that operates an accident towing licence.

These costs are broadly made up of capital and operating costs (where operating costs cover both labour and non-labour costs). Fixed costs will be calculated in total for the business as they are fixed costs shared across regulated and non-regulated services. Variable costs will be calculated for the regulated services provided under the licence.

In each section, a simple formula is provided for each individual cost. These formula result in a set of data and assumptions that are covered in detail in Section 1.6.

1.3.1 Fixed costs

1.3.1.1 Licence holding cost

The industry has a genuine opportunity cost relating to the accident towing licence. Reportedly, acquiring a licence can cost over $300,000.[2] While the licence can be transferred, pending approval, licence transfer applications have declined in recent years, from 27 (19 approved) in 2018 to 12 (11 approved) in 2020.[3]

In a given year, the cost relating to licence holding can be calculated as follows:

$$licence\ cost = (cost\ of\ licence) \times (cost\ of\ capital)$$

This cost is separate to annual licence fees, which are an additional fixed cost.

1.3.1.2 Vehicle

The capital cost of a vehicle is a significant cost for the accident towing industry. The annual cost can be estimated based on both the cost of capital and depreciation, assuming that vehicles are, on average, halfway through their useful lives and depreciation is calculated according to a straight line approach.

$$vehicle\ depreciation = \frac{(cost\ of\ vehicle)}{(useful\ life\ of\ vehicle)}$$

$$vehicle\ financing\ cost = \frac{(cost\ of\ vehicle)}{2} \times (cost\ of\ capital)$$

1.3.1.3 Land and buildings

Land and buildings costs for office and other space can be calculated based on market rental rates, as follows:

$$office\ building\ costs = (average\ office\ area\ sqm) \times (market\ rent\ per\ sqm\ including\ outgoings)$$

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[2] Pointon Partners, *Buying, selling and moving accident tow truck licences in Victoria* (2017); link available

[3] Source: Victorian Department of Transport

1.3.1.4 On-call driver cost

Regardless of whether or not a driver is allocated to an accident tow, a business needs to have drivers on call at all times to provide towing services on short notice.

On call costs can be calculated based on the total time required for drivers to be on call throughout the year multiplied by average driver wages, as follows:

$$on\ call\ costs = 365 \times 24 \times (average\ hourly\ on\ call\ wage\ for\ vehicle\ operator) \times (average\ on\ call\ vehicle\ operators\ per\ licence)$$

1.3.1.5 Back office staff support

Back office support, such as completing administrative work and handling calls, must be supplied to facilitate timely and safe delivery of accident towing.

Support costs can be calculated based on the total time required multiplied by average driver wages, as follows:

$$back\ office\ staff\ support\ costs = (average\ annual\ support\ staff\ wage) \times (average\ number\ of\ support\ staff)$$

1.3.1.6 Corporate overheads and taxation

Corporate overheads include all shared costs such as management, insurances, electricity, IT systems and similar. Taxation is a significant cost to the accident towing industry.

Given the broad range of costs included, we suggest that this category be based on a mark-up percentage on other fixed costs.

1.3.2 Variable costs

The approach taken here in relation to variable costs has been informed by the approach adopted to adjust benchmarks in the ESC's 2018 accident towing decision.[i]

It is important to note that variable accident towing costs on a per hour basis will also be significantly dependent on the length of call outs, which in turn is largely dependent on the congestion conditions on Melbourne's roads.

1.3.2.1 Labour (vehicle operator)

Vehicle operator costs can be calculated based on the total time for each accident tow multiplied by average driver wages, as follows:

$$labour\ (vehicle\ operator)\ costs = (average\ total\ time\ per\ accident\ tow) \times (average\ annual\ number\ of\ allocations\ per\ licence) \times (average\ operator\ wage\ above\ on\ call\ wage) \times (average\ operators\ per\ truck)$$

In addition, to enable calculation of the after-hours cost (and price), implementation of this calculations would need to take account of the proportion of time accident tows are made in standard hours compared to after hours.

1.3.2.2 Non-labour (vehicle fuel and consumables)

Vehicle fuel and consumables costs can be calculated based on the total kilometres travelled by each vehicle using standard cost assumptions available from sources such as the Australian Transport Assessment and Planning (ATAP) Guidelines,[ii] as follows:

$$\begin{aligned} &vehicle\ fuel\ and\ consumables\ costs \\ &\quad = (average\ accident\ tow\ distance) \\ &\quad \times (average\ annual\ number\ of\ allocations\ per\ licence) \\ &\quad \times (average\ vehicle\ operating\ cost\ per\ km) \end{aligned}$$

For the purpose of this calculation, the "average accident tow distance" is the distance from the depot via the accident scene to the tow destination.

1.3.2.3 Non-labour (vehicle maintenance)

Vehicle maintenance costs can be calculated based on the total kilometres travelled by each vehicle using standard cost assumptions available from sources such as the ATAP Guidelines,[iii] as follows:

$$\begin{aligned} &vehicle\ maintenance\ costs \\ &\quad = (average\ accident\ tow\ distance) \\ &\quad \times (average\ annual\ number\ of\ allocations\ per\ licence) \\ &\quad \times (average\ vehicle\ maintenance\ cost\ per\ km) \end{aligned}$$

For the purpose of this calculation, the "average accident tow distance" is the distance from the depot via the accident scene to the tow destination.

1.3.3 Adjusting for non-regulated service provision

After establishing the total cost of accident towing service provision, the next step is to account for the fact that some portion of the fixed costs can be used to provide non-regulated services.

By splitting the previous calculations into fixed and variable costs, the adjustment can be fairly simple, as follows:

$$\begin{aligned} &annual\ cost\ of\ regulated\ service\ provision \\ &\quad = (fixed\ costs) \times (regaulted\ utilisation\ rate) + variable\ costs \end{aligned}$$

1.4 Storage costs

The costs of storage could be calculated separately, in a similar way to the method proposed by VACC in its submission on the ESC's 2018 consultation paper.[4] In summary, the approach took into account the following costs:

- administration costs, including labour
- industrial property leasing costs per square metre (including outgoings)
- a reasonable rate of return (a set percentage profit margin)
- bad debts associated with outstanding storage fees (assume storage losses on a set percentage of uncollected vehicles).

[4] VACC, *Review of accident towing and storage fees 2018* (May 2018); link available

1.5 Price setting

After calculating each of the annual values above, the total annual cost can then be mapped to prices based on some straight-forward cost allocation principles. These cost allocation principles could be agreed between industry, stakeholders and the ESC but could include that:

- the base fee should aim to recover fixed costs
- the additional per kilometre fee should aim to recover variable costs
- storage fees should recover costs directly associated with providing storage.

Once costs are allocated the cost can be divided by the expected number of allocations to determine the specific price.

1.6 Data sources

Based on the simplified formulas provided above, it is possible to identify the data and inputs that would be needed for the approach to be implemented. We have then allocated these to either being likely to be publicly available or requiring input from industry, likely via a brief survey.

Deloitte Access Economics notes the ESC's concerns expressed in its 2018 final report regarding challenges related to cost surveys, including that undertaking a cost survey can be a costly and burdensome exercise.[iv] Consequently, we recommend that relevant public cost indices be relied upon as far as is possible and reasonable.

1.6.1 Sourced from publicly available information

The following data types are likely to be available from public information:

- (cost of capital) – a simple cost of capital calculation that include a market return on investments and a cost of corporate debt (such as commercial bank loan rates) may be appropriate
- (useful life of vehicle) – standard values such as those available from the ATO may be appropriate
- (market rent per sqm including outgoings) – market real estate reports would provide useful sources of information (e.g. *Savills Research – Q1 2021 Quarter Time National Industrial* for industrial property lease costs across Melbourne)[v]
- (average annual number of allocations per licence) – this data is available from VicRoads[vi]
- (average accident tow distance) - can be estimated based on response time requirements and depot locations
- (average vehicle operating cost per km) – available from sources such as the ATAP Guidelines for the relevant vehicle category[vii]
- (average vehicle maintenance cost per km) – available from sources such as the ATAP Guidelines for the relevant vehicle category.[viii]

1.6.2 Industry survey

The following data types are likely to require input from the accident towing industry directly:

- (cost of licence)
- (cost of vehicle)
- (average office area size)

- (average hourly on call wage for vehicle operator)[5]
- average operator wage when responding to tow (above on call wage)
- (average number of on call vehicle operators)
- (average operators per truck)
- (average annual support staff wage)[6]
- (average number of support staff)
- (overhead mark-up percentage)
- (annual cost of taxation) (unless data sourced publicly)
- (average total time per accident tow)
- (utilisation rate) – what percentage of the time is an accident towing business's staff and truck working on accident towing rather than all other parts of the business (similar to that recognised by IPART in 2014, the extent of utilisation affects the hourly cost and the amount that an operator must charge for cost recovery)[ix]

1.7 Limitations of this approach

While public data indices offer useful insights into the general nature of changes in business costs, none of them are specific to the accident towing industry. Indeed, the *Accident Towing Services Act 2007* (Vic) itself uses changes in the Melbourne Transport CPI as the basis for annual fee adjustments, despite many industries included in the index having different operating models and functions, and varying cost bases to the accident towing industry. However, many of the costs faced by the accident towing industry (e.g. labour costs) are shared in common with other industries.

The cost-of-service methodology also has geographic limitations. For example, industrial premises lease costs vary depending on depot location. In addition, there will be variability in distances travelled by operators during a call out, depending on depot location.

The approach above is based on a realistic efficient industry operator. Some operators will have higher costs while others will have lower costs.

The approach could lead to significant changes in the mix of fixed and variable fees per accident tow. This may require some transitional arrangements, although because most customers of accident towing are not 'ongoing' and have not made investment and consumption decisions based on existing prices, then a relatively rapid transition should be possible.

The utilisation rate could change over time depending on circumstances in the unregulated towing market. A conservative value for the utilisation rate would be required to ensure that regulated service providers are able to recover efficient costs of providing a regulated accident towing service.

1.8 Next steps

Deloitte Access Economics understands that VACC would be willing to work closely with the ESC and other stakeholders to establish this approach, including assisting with data identification and collection.

Further, the model set out here is unlikely to be complete and is likely to need further refinement.

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[5] This data may potentially be available in public data.
[6] This data may potentially be available in public data.

2 Productivity performance

2.1 Background

As well as the four-yearly reviews recommending changes to accident towing, storage and salvage fees, annual adjustments are also applied to fees on 1 July of the interim years. These adjustments are currently set at 0.5 per centage points below the transport industry CPI for Melbourne, further detail is provided below.

The purpose of these adjustments is to both account for ongoing cost increases (the CPI component) and to provide incentives for firms to achieve productivity gains. The goal is to allow firms to recover general increases in costs that may arise from year-to-year but to provide additional incentives to achieve productivity improvements.

The inclusion of the productivity adjustment in the accident towing fee adjustment mechanism aims to mimic outcomes of competitive markets where firms naturally have incentives to achieve productivity gains to increase returns, and those gains are shared with consumers in the form of lower prices and/or improved service quality.

Upon review of the previous fee benchmarking and productivity review submitted by Advisian in 2018 to the ESC,[x] we are providing updated analysis of relevant data whilst following aligned methodology.

2.2 Productivity adjustment methodology overview

The annual adjustment mechanism applied to regulated accident towing fees is in the form of a 'CPI minus X' formula specified in the Act, where:

- 'CPI' is the percentage change in the Melbourne transport consumer price index (using the March quarter values of the prior two financial years)
- 'X' is a productivity adjustment figure (currently set at 0.5 per cent and reviewed by the Commission every four years).

Fees are calculated as:

$$A \times \left(\frac{B}{C} - X\right)$$

where:

- 'A' is the fee for the previous financial year
- 'B' is the most recent March quarter value of the Melbourne transport CPI
- 'C' is the March quarter value of the Melbourne transport CPI for the previous year
- 'X' is the productivity adjustment figure.

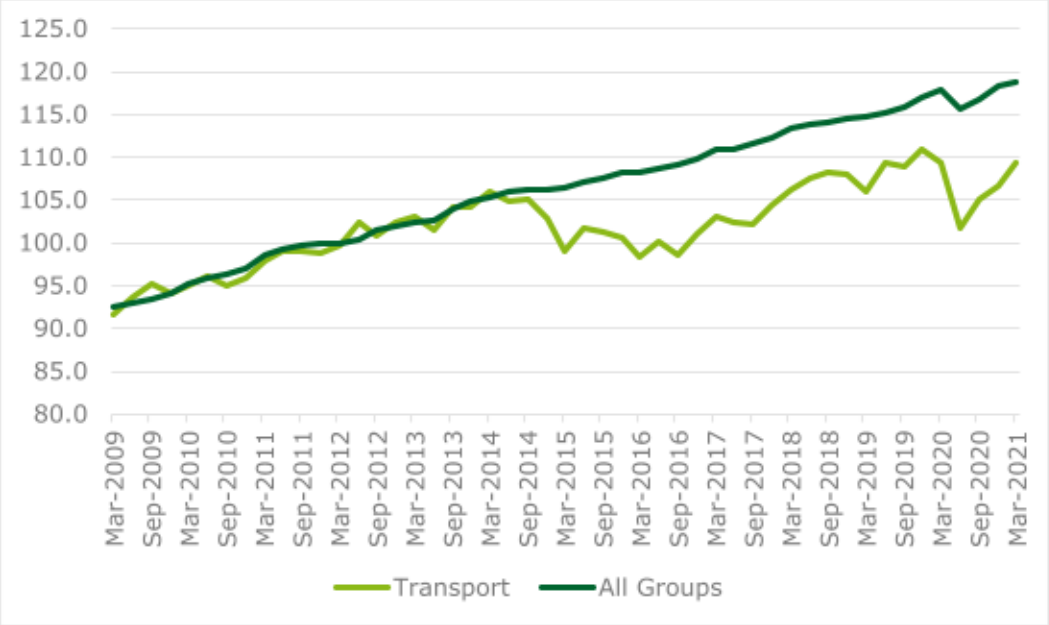
The Act also places a 'zero floor' on the CPI minus X adjustment, meaning fees remain unchanged in a given year if application of the CPI minus X formula would reduce fees.

The Commission is required to review the productivity adjustment figure in its four-yearly reviews and make a recommendation to the Minister as to what value should be set until the next review. The Act specifies that, in the absence of a recommendation by the Commission, the figure is to be 0.5 per cent.

2.3 Overview of the Melbourne Transport CPI and other related metrics

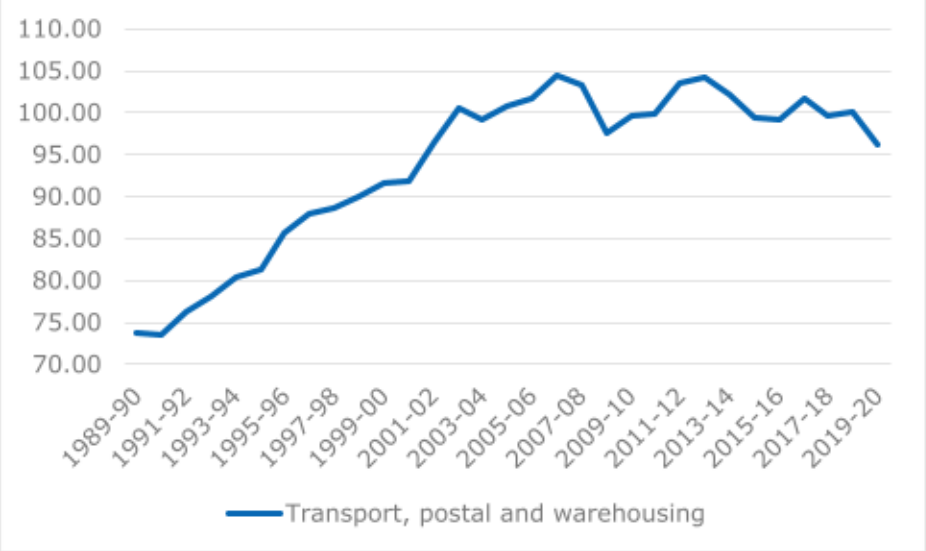
The Melbourne transport CPI measures changes in the purchase price of a basket of goods and services in the transport sector. As shown in Figure 1, the transport group CPI has begun to trend below the levels of all groups CPI in Melbourne since 2014, with a far more significant dip during 2020, largely due to reductions in fuel costs associated with the initial response to COVID-19 and OPEC pricing decisions. Almost all of this 'dip' has since been recovered.

Figure 1: Melbourne CPI Trend 2009-2021



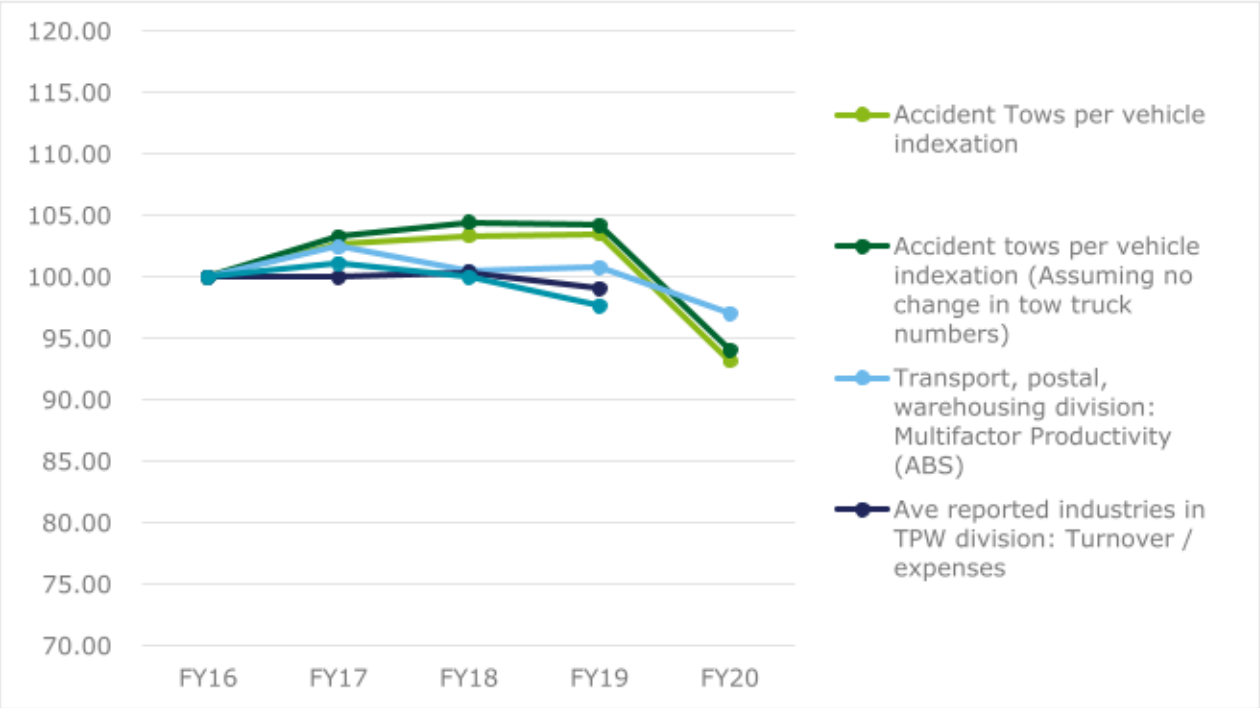
The ABS maintains historic records of multifactor productivity for the Transport, Postal and Warehousing division from 1989-1990. Productivity gains were consistently achieved by the division through the 1990s and into the early 2000s, yet productivity has been relatively volatile according to this measure in more recent years, with no ongoing improvement and has actually declined overall since the early to mid-2000s, as shown in Figure 2.

Figure 2: Historic Trend in multifactor productivity for the Transport, Postal and Warehousing Division



In comparing multiple metrics using the 2015-16 financial year as a baseline, Figure 3 shows the broad range of potential productivity measures for the industry. This finding is very similar to that in previous research by Advisian which showed a broad range of productivity outcomes ranging from positive to negative. In particular, on one hand, there has been a severe decline in accident tows per vehicle as a result of the drop off in accident towing per vehicle over COVID-19. Even on the upper side of productivity indices since 2016, there has been a decline in transport, postal, warehousing (TPW) division multifactor productivity, as well as the ATO data showing turnover as a percentage of expenses for towing services and the TPW division.

Figure 3: Comparison of Productivity Measures



Source: VicRoads, ABS, ATO

Based on this update to the approach taken by Advisian in the 2018 review, we have similar findings that there is a range of potential productivity outcomes, depending on the data that is used. However, it appears that, since 2018, there has not been any sustained improvement in productivity in the industry and that the impact of COVID-19 is likely to far outweigh any productivity gains that have been made.

Endnotes

[i] ESC, *Review of Accident Towing and Storage Fees Final Report*, December 2018; link available

[ii] Chapter 5, "Vehicle operating cost (VOC) models", *Australian Transport Assessment and Planning (ATAP) Guidelines*; link available

[iii] Chapter 5, "Vehicle operating cost (VOC) models", *Australian Transport Assessment and Planning (ATAP) Guidelines*; link available

[iv] ESC, *Review of Accident Towing and Storage Fees Final Report*, December 2018, p. 29; link available

[v] An example of such a source is *Savills Research – Q1 2021 Quarter Time National Industrial*; link available

[vi] VicRoads, "Monthly statistics showing tow truck accident allocations"; link available

[vii] Chapter 5, "Vehicle operating cost (VOC) models", *Australian Transport Assessment and Planning (ATAP) Guidelines*; link available

[viii] Chapter 5, "Vehicle operating cost (VOC) models", *Australian Transport Assessment and Planning (ATAP) Guidelines*; link available

[ix] *VACC submission Review of accident towing and storage fees 2018 Essential Services Commission*, May 2018, p 4; link available

[x] Advisian, *Accident towing fees in the Melbourne Controlled Area Fee benchmarking and productivity review*, June 2018; link available

Limitation of our work

General use restriction

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