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IVEY

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BECK TAXI

R Chandrasekhar wrote this case under the supervision of Professor Srinivas Krishnamoorthy solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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It was May 25, 2009. Gail Beck Souter, chief executive officer (CEO) of Beck Taxi (Beck), the leading taxi brokerage with the highest number of cabs in the city of Toronto, Canada, was facing a pricing challenge. The summer season, lasting three months, was about to begin. Summer was a lean season for the taxi trade because educational institutions were closed, people were on vacation and many in the community preferred to walk, cycle or take public transport. "Is this the time," Souter wondered, "to reduce the radio fee?"

The radio fee was required in exchange for Beck's providing radio dispatch service to individual taxi drivers driving vehicles bearing Beck's colors. The fee could be restored, she thought, at the beginning of the fall season. Simultaneously, Souter was weighing a few other options. One option was a simple increase in the fees. Another option was to move to a two-part fee structure, wherein the drivers would pay a fixed fee in advance and then pay a variable fee for each Beck dispatch.

Souter knew that any decision on her part, other than status quo, would have ramifications for the whole cab industry in Toronto. Taxi drivers, competing taxi brokerages, vehicle owners and license plate holders would all be affected by a change in Beck's radio fee.

CAB INDUSTRY IN TORONTO

Toronto had a total of 4,851 cabs. At one cab for every 500 Torontonians, as opposed to one cab for every 1,000, which was the ratio in most metropolitan cities around the world, Toronto's cab industry had a supply overhang. Beck was the largest among the Toronto cab companies (more commonly known as brokerages), with a fleet of 1,476 vehicles. The cab service in general was commoditized because the vast majority of customers wanted no more than the first available vehicle. However, individual brokerages sought differentiation through personal touch points and brand value. For example, Beck had started, two weeks earlier, airing a commercial in city's TV channels to reinforce its brand equity.

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Toronto had three autonomous players in the cab industry: Municipal Licensing & Standards (ML&S), brokerages and cab drivers.

Municipal Licensing &Standards

Municipal Licensing & Standards (ML&S), a division of the Toronto municipal government, was a regulatory body with five major responsibilities relating to the cab industry: issuing taxi licenses to vehicles, issuing taxi licenses to drivers, determining and capping the number of taxi licenses, fixing the fares charged to taxi customers and conducting training classes for taxi drivers. ML&S was mobilizing $8 million in revenue every year through an annual taxi driver license renewal fee of $836 per driver. The taxi vehicle licenses (more popularly known as "plates") were independent of the licenses issued to taxi drivers. The fee for a plate was $5,681, payable at the time of licensing.

The most recent revision of cab fare in Toronto had occurred in June 2008. Since then, taxi fares were linked, as before, to the distance covered: the fare for the first 0.155 kilometers was $4 and increased $0.25 for each additional 0.155 kilometers. The fee for waiting time for a cab, while in engagement, was $0.25 for every 31 seconds. The customer could negotiate a flat rate (to the airport in particular) according to the rate sheet available from the driver and approved by the brokerage (see Exhibit 1).

The plate included property rights that were recognized by law; therefore, a plate holder could keep the plate in the family forever, passing it from one generation to the next. The plate could also be bought and sold in the open market, at a premium. In February 2009, each plate had a market value of $200,000. Plate holders were renting out their plates at an average fee of $1,150 per month to a driver. Many plate holders collected their rents through intermediaries known as designated agents. The plate holders did not actually own the plates; the city of Toronto did. Thus, banks could not use the plate as collateral for the lending of money to a plate holder.

ML&S issued three types of plates: Ambassador (for owner-driven vehicles), Accessible (for cabs carrying passengers with special needs) and Standard (for individuals, companies and drivers). The ML&S had issued 1,403 Ambassador licenses, 85 accessible licenses and 3,448 standard licenses. Of the standard license holders, 809 had no agent or lessee, 1,474 had an agent but not a lessee, 534 had a lessee but not an agent and 631 had both an agent and a lessee.[1] M&LS had not issued any new Standard plates for the last 12 years.

ML&S had recently introduced three important changes with regard to licensing plates. A standard plate could be sold only to a licensed cab driver. An individual could hold only one plate at a time. On the death of a plate holder, the plate was held in trust for one year before it could be passed to a designated heir.

Brokerages

The cab industry in Toronto consisted of 35 brokerages operating a total of 4,851 vehicles. A brokerage played two roles: operating a dispatch service and managing a number of plates, each attached to a vehicle. A brokerage did not usually own plates; instead, it managed the plates for investors who authorized the brokerage to lease them out. In return, the brokerage paid the plate holder a regular fee.

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[1] *Sara Abraham et al., Toronto Taxi Drivers: Ambassadors of the City — A Report on Working Conditions, University of Toronto, Toronto, January 2008, referenced March 9, 2008. Note: the data was current as of October 2006.*

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The brokerage leased each plate to drivers in one of two ways: either on a per-shift basis (sometimes for up to a week at a time) to shift drivers who would vary each shift (or week) or on a long-term basis to a single driver who maintained control of the vehicle and was responsible for maintenance and repairs. Often in the latter case, the driver had purchased the vehicle but had signed the ownership over to the plate holder to comply with an ML&S bylaw that required the plate and car be leased together and not separately.

Plate holders (or lessees) using a brokerage company were required to paint their cars in the colors of the brokerage company. A customer calling a dispatch service had no way of knowing whether the driver picking them up was an owner-operator, a lease driver or a shift driver.

Every brokerage attracted plates, fleet and drivers because of the radio business it offered and the company's brand value. The radio business consisted of a 24/7 dispatch service (through either a two-way radio or computer dispatch). The brokerage also hired a pool of customer service representatives (who handled phone orders), dispatchers (who connected customers with the drivers on call), sales staff (who generated corporate clients) and road supervisors (who ensured that vehicles were in good running order). Although driving the cab was a large component of the business, considerable back-end work was involved in not only getting the customer into the cab but in keeping the customer loyal to the brokerage.

Drivers

A total of 9,898 licensed drivers operated 4,851 vehicles 24/7 in two 12-hour shifts. Put simplistically, the drivers provided the labor, while the plate holders and brokerages provided the capital. Although cab drivers were regulated by the government, they did not have the protection of employment standards legislation. Because cab drivers were considered self-employed, they were not entitled to either a minimum wage or benefits. They were also not on the payroll of the cab companies and had the freedom to move from one cab company to another at will. Most drivers did not own the vehicles they drove.

A cab driver would usually receive 12 to 15 fares in a daytime shift. The average fare was between $10 and $15. Drivers often received a tip of approximately 10 per cent, as an add-on, especially on longer routes. Drivers needed to have a sense of where potential passengers would congregate in the city on any particular day. For example, a hockey night was a big draw. Parking at cab stands, some designated by law, was another way of catching fares. Cab stands, which were typically located at the outskirts of malls and transit centers, helped aggregate both supply and demand for cab service.

Drivers could be divided into two kinds: shift drivers (who leased a plate on a shift basis) and lease drivers (who had a long-term lease on a vehicle). Shift drivers paid a fee of $65 per shift (or $400 per week), whereas lease drivers paid $1,150 per month toward leasing the plate. The fee was paid either directly to the plate holder, or, more frequently, to an agent that was often a brokerage. In addition to the lease fee, lease drivers were responsible for running costs (such as gas and traffic tickets) and maintenance costs (such as repairs) of their vehicles. They also paid a monthly fee to a brokerage toward the cost of its dispatch services. Lease drivers often rented their cab to another driver for a night shift. Shift drivers usually did not pay for maintenance, but they paid for running costs from their own earnings.

Toronto was a phone-order market. Cruising for a fare was therefore not common among drivers. This situation did not, however, pre-empt idle time because drivers incurred unpaid mileage when picking up a phone order or when returning to a stand after a drop-off. In a phone-order market, such as in Toronto, the speed of the response was an index of customer service, as opposed to a hail market, such as in New York or Mumbai.

COMPANY BACKGROUND

Beck Taxi, a family-owned company, was founded by Jim Beck in May 1967. Its vehicles carried distinctive orange and green colors. At the start of his business, Jim Beck owned and operated 25 cars from a garage on Edward Street. He wanted customers to be able to get a cab within five minutes. Beck and his drivers split the daily earnings 50:50. In the early 1970s, the company started dealing with vehicles outside of those it owned. It charged a fee of $100 per month for the dispatch service. By about 1980, Beck ceased to own vehicles and became a sole radio dispatch service, charging a fixed radio fee of $375 per month, stepping it up to $400 per month in 1989. The company had not increased the fee since then.

The fleet had vastly expanded under the leadership of Souter, the founder's daughter, who had taken over the business on the death of Jim Beck in August 1985. By processing more than 22,000 calls in a 24-hour period, the company was making more than half a million dispatches per month.

Beck had four categories of account holders: corporate, government, insurance and personal. Account holders required no minimum charge and were charged only for the services received. The company had four full-time customer service advisors on the road, ensuring that all Beck vehicles were washed, clean and in good mechanical condition.

Beck had between 2,500 and 3,000 drivers on call, at any time, averaging two drivers per vehicle in its fleet, covering a 12-hour shift each. Approximately 35 per cent of drivers were transient, leaving a pool of approximately 60 per cent as the core group of drivers. Some drivers had been driving Beck vehicles for more than 20 years. They were independent contractors, each paying $450 per month to the company, comprising $400 for radio fees, $20 for GST and $1 for Beck's Drivers' Assault Fund (all of which were mandatory fees) together with $19 for a pager and $10 for a point-of-sale (POS) terminal (both of which were optional). Each newly enrolled driver had to undergo sensitivity training, which addressed the needs of people with disabilities. Since 1994, more than 9,000 contractors had taken the training program. The company had 150 full-time employees, of whom 50 were dispatchers, assigned to the 10 radio frequencies for the almost 100 zones that the city had been carved into. The remaining 90 employees were administrative staff and call center operators, who received customer calls and sent them to dispatchers.

BROKERAGE ECONOMICS

Several factors affected the economic viability of Beck as a brokerage. Beck provided radio service to each of the 1,476 plates it managed. Independent owners owned 576 plates, and 900 plates were part of larger fleet of vehicles, each fleet consolidated into a single agency, often a garage. The largest brokerage had a fleet of 155 vehicles, and the smallest brokerage had two vehicles. To increase the number of plates it managed, and, thus, generate higher revenues through the monthly radio fee, Beck targeted the fleet owners with some incentives. For example, it would provide every tenth car, from the same pool of consolidation, free service by way of dispatch. Thus, Beck offered a 10 per cent price discount to grow its fleet size by an additional 10 vehicles.

Although cruising for fares was not common among cab drivers in Toronto, they commonly "played the street" rather than "playing the radio," as the trade terminology went. These drivers would bypass the dispatch service and pick up fares from cab stands outside traffic terminals. Pickups were a major part of a driver's earnings, often 70 per cent, if the zone of operation was downtown where the traffic was not only dense but had several designated pockets aggregating the demand for cab service. This bypass did not reduce the brokerage's earnings from each driver, which were fixed. However, this practice had led

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Souter to consider that the driver's earnings could, in some way, be linked to the usage of the dispatch service, which was specific to Beck. One way to link earnings to the dispatch service would be to charge a fixed fee, of say fifty cents or a dollar, each time the driver used Beck's dispatch service. The amount would be irrespective of the fare on the meter.

Such a linkage, however, had an element of contradiction. A major part of building revenues was to ensure that more and more plate owners moved to Beck (from other brokerages), and more and more drivers used Beck's dispatch service. Such a context provided no rationale for charging a usage fee. A fee could, in fact, likely reverse the flow. Drivers could leave Beck and seek partnerships with other brokerages, defeating Beck's larger goal of building a pool of core drivers.

Souter believed the situation could be rectified if the fixed fee could be reduced, even with a fee charged each time the dispatch service was used. A reduction in the monthly radio fee — a major cost for the driver — would be an incentive for drivers to sign up with Beck. Such a reduction would also open up several options for pricing the radio fee.

Souter wondered, however, whether charging a radio usage fee would create a logistics "nightmare" for Beck's internal operations. Keeping track of each individual usage of dispatch service of 1,476 vehicles driven by 2,500 to 3,000 drivers on call in every shift, day and night, and crediting their accounts monthly appeared a daunting task. The issue was compounded by the fact that drivers paid the radio fee in advance every month. The payment was conditional to activating the radio for usage in the vehicle.

PRICING OPTIONS AND IMPLICATIONS

Souter had four options for consideration: 1) maintain the status quo, 2) increase the fixed fee, 3) reduce the fixed fee and change a fee for each dispatch, or 4) reduce the fixed fee only for the summer.

Maintain the Status Quo

Beck was already the market leader. Its fleet size was more than three times the size of its nearest competitor, Diamond Taxi, which had 475 vehicles. Continuing with the current pricing structure would not in any way dilute, in the foreseeable future, its near-total control over the taxi trade in Toronto. The brokerage had also released a TV commercial in May 2009, which would reflect positively on its brand equity. The commercial would influence not only consumers but also potential drivers considering a switchover from their existing brokerage. But, at the same time, Beck could afford, as the market leader, to take the risks, if any, of altering its pricing structure and thereby changing the dynamics of the cab industry in Toronto.

Increase the Fixed Fee

Increasing the fixed fee would be a revolutionary step on several grounds. According to a general perception, Toronto cab drivers were an exploited lot, working long hours without any statutory safeguards, such as a minimum wage. An increase in the dispatch fee would be seen as cutting into their incomes, already perceived as low. At the same time, the last price increase had been more than a decade ago, providing a justification for a fee increase.

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Reduce the Fixed Fee for the Radio and Charge a Fee for Each Dispatch

Souter was aware that several combinations would be possible in this option. The fixed fee could be reduced from the current level of $400 by blocks of $25. The usage fee could be fixed, irrespective of the fare amount, or it could be variable, calculated as a percentage of the fare amount.

Reduce the Fixed Fee Only for the Summer

The fixed fee could be reduced during summer months without the need to charge a usage fee. This move, Souter thought, would likely encourage more drivers to transfer their allegiance to Beck and would give Beck an opportunity to test the waters before making a larger change in pricing.

DECISION

As Souter reflected on the pricing problem, she couldn't help feeling that an economic analysis of the options would help. Of course, she would not let her decision be dictated by pure financial consideration. She was just not comfortable with the idea of introducing a scheme that would make money for the company but hurt the taxi drivers during these difficult economic times. Perhaps the radio fees could be structured in a manner that would benefit both the drivers and the company.

Exhibit 1

TORONTO'S MUNICIPAL LICENSING & STANDARDS' TAXI TARIFF

TORONTO

Municipal Licensing and Standards

TAXICAB TARIFF "A"

IMPORTANT PUBLIC NOTICE

The driver cannot recommend hotels or restaurants unless requested to do so by the passenger. For information, call Tourism Toronto at **416-203-2500.**

For a compliment or complaint call: 1-877-TO-TAXIS or e-mail: taxiline@toronto.ca

CAB NUMBER/OWNER:

02992D

BALAMURUGAN, NARAYANASAMY

GOODS AND SERVICES TAX INCLUDED IN FARE

- By distance: One to four passengers
- For the first .155 kilometer, or part thereof $4.00
- For each additional .155 kilometer, or part thereof ..... 25¢
- For each additional passenger in excess of four $2.00
- For each thirty-one (31) seconds of waiting time while under engagement ..... 25¢

BAGGAGE

- Wheelchairs, including loading and unloading by driver ..... no charge
- Charges for trunks and other items not covered by this tariff shall be agreed upon before commencement of trip.
- For delivery of any parcel, document, or thing, where no passenger is carried – minimum charge per trip $10.00

- **If meter is not on, the ride is free.**
- **Pre-approved flat rates to the airport are available. Ask driver for rate sheet.**
- **Meter rate will apply if less than flat rate.**

Source: Company files