

Interim Review of Tow Rates

Date:	May 15, 2012
To:	Licensing and Standards Committee
From:	Executive Director, Municipal Licensing and Standards
Wards:	All
Reference Number:	P:\2012\Cluster B\MLS\LS12009

SUMMARY

The purpose of this report is to respond to the direction from City Council to consult with the tow truck industry and other pertinent stakeholders, and to make recommendations with respect to tow truck rates, providing a rationale and criteria for such recommendations.

Accident tow rates were last reviewed in 2006. At that time, the rates were increased by 10.5%, in accordance with the indexing model developed in consultation with the tow industry. This model is the same one used in the October 2011 report from the Executive Director, Municipal Licensing and Standards ("ML&S"), which included a recommendation to increase accident tow rates by 21.6%.

As a result of the consultations and research conducted, staff conclude that there are a number of different business models in the industry with considerably different cost structures and that these cost structures are tied to overall industry conditions and regulations. As a result, a proper review of tow rates must include a comprehensive review of the regulatory regime for the industry as well as the prevailing industry conditions.

Fuel costs, which are a major cost driver for tow operators, have risen over 50% in the past six years. For this reason, staff recommend that an interim increase of 2.0% be approved by Council. This figure represents the average of the annual rates of increase in the all-items CPI for the Toronto area for the period 2005-2011. Staff recommends that the increase take effect immediately. As a component of the full industry review, ML&S will work with Corporate Finance to develop a comprehensive model to assist in the validation of base tow rates, and will report back in 2013.

This report was prepared in consultation with the Corporate Finance Division.

RECOMMENDATIONS

The Executive Director, Municipal Licensing and Standards, recommends that:

1. City Council increase accident scene tow rates on major highways from \$188.00 to \$192.00 (an increase of 2.0%, rounded to the nearest dollar);
2. City Council increase accident scene tow rates on city streets from \$166.00 to \$169.00 (an increase of 2.0%, rounded to the nearest dollar); and
3. City Council increase private property tow rates from \$88.00 to \$90.00 (an increase of 2.0%, rounded to the nearest dollar).

Financial Impact

The additional revenue generated by the increase in the rates will be collected by tow truck operators and will partially offset their increased costs. As such, there is no financial impact to the City as a result of the recommendation in this report. The recommended interim increase of 2.0% is based on the average of the annual rates of increase in the all-items CPI for the Toronto area for the period 2005-2011.

There is no financial impact to the City as a result of the recommendation in this report, as the proposed amendments pertain to rates charged to the public by the tow industry.

The Deputy City Manager and Chief Financial Officer has reviewed this report and agrees with the financial impact information.

DECISION HISTORY

City Council on April 10 and 11, 2012, referred the report on fees for accident tows and tows from private property, from the Executive Director, Municipal Licensing and Standards ("ML&S"), for review and consultation with the tow truck industry, insurance companies and brokers, the Canadian Automobile Association (CAA) and other interested stakeholders. It additionally directed the Executive Director, Municipal Licensing and Standards to report to the Licensing and Standards Committee meeting on May 25, 2012, such report to include the review criteria for assessing and/or recommending any fee changes.

Decision: <http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2012.LS12.2>

ISSUE BACKGROUND

At the April 2012 Licensing & Standards Committee meeting, the Committee received the deferred report from the October, 2011 meeting from the Acting Executive Director, ML&S, which had recommended an increase of 21.6% to a blended rate which captured both highway and city street tow rates, and which was based on a cost indexing model developed in consultation with the tow industry in 2006.

This model was based on four key cost drivers for the tow industry: fuel, insurance, vehicle, and maintenance. These cost drivers were provided by the Metropolitan Towing Committee in a study entitled "Towing Rate Study 2011." The Metropolitan Towing Committee represents a number of tow truck industry stakeholders. The weightings derived from the study were then applied to the change in the Consumer Price Index (CPI) for each cost driver, thus providing an estimate of the overall change in the cost of operating a tow truck in Toronto.

There is currently no existing model to address the establishment and validation of the base rate costs for these services. The development of this model will be undertaken in the context of the review.

COMMENTS

Staff undertook to review its cost indexing model by reviewing the approaches taken by other jurisdictions in establishing tow rates and by consulting with the industry and other relevant stakeholders.

No consistent approach to setting towing rates across GTA municipalities

In reviewing other jurisdictions within the GTA, staff found that tow rates in Toronto were generally lower than in surrounding municipalities. In addition, most municipalities do not use any specialised formula to come up with their tow rates. Brampton, which set its rate at \$200 in 2001, did so on the basis of industry consultations and is currently undergoing a review of its rates. Mississauga, which most recently set its rate at \$237 (plus \$103 for winching), determines increases by applying the rate of increase to the All-Items CPI. Mississauga reviews its rates annually. Vaughan, which does not use a formula, set its rate at \$250 (plus up to \$100 for off-road recovery) and is also currently reviewing its rates. Markham licenses tow trucks, but does not set rates. Richmond Hill does not license tow trucks. Hamilton does not currently license tow trucks but its City Council has backed a proposal to do so. However, the proposal does not include setting rates.

None of the municipalities surveyed had a quantitative model for determining the initial base rate or for calculating a periodic rate adjustment.

The City's Indexing Model

As part of its review, staff conducted two consultations with participants related to the towing industry and two consultations with other relevant stakeholders (including the insurance industry, the CRC, and CAA).

Participants were asked to provide a critical review of the City's existing indexing model, as outlined in Table 1.

Table 1
Tow Truck – Key Operating Drivers
Relative Weighting and Changes to CPI

A	B	C	D	E	F
Cost Driver	Index - item	Change in CPI 2005-2011	2011 Cost of Operation	2011 Weighting	Weighted Change (C x E)
Fuel – Diesel (replaces gas)	CPI- Toronto - Diesel	50.5%	\$30,720 ¹	34.7%	17.5%
Insurance	CPI- Toronto – Insurance Premiums	44.2%	\$11,500 ²	13.0%	5.7%
Vehicle Price	CPI- Vehicle Prices	-7.4%	\$38,193 ³	43.1%	-3.2%
Maintenance	CPI- Toronto – Vehicle Maintenance	16.2%	\$8,200 ⁴	9.3%	1.5%
TOTAL		--	\$88,613	100%	21.6%

Notes:

¹Fuel cost based on 80 litres per day over 300 days at an average price of \$1.28.

²Insurance premium based on information from tow industry.

³Vehicle price given as \$126,500; annual cost is based on amortized monthly payments over a 4-year term at 8% interest.

⁴Maintenance related expenses based on information from tow industry.

Consultation with the Tow Industry and Other Stakeholders

Fuel

Tow truck operators are distinguished between tow operators that provide a range of towing services, including road-side assistance and tow operators that are largely dependent on accident tows. The former group will generally attend a collision scene as a

result of a call by a customer. The latter will generally attend a collision scene as a result of monitoring the airwaves and identifying accidents in their vicinity. Staff were told that a tow truck engaged in more diversified work may, in the course of a day, deal with 8-10 calls, often driving from one call to the next. Tow trucks dedicated to collisions will more often sit near highway access points, or other spots that provide convenient access to areas where collisions occur with more frequency. These tow trucks are also more likely to be idling their engines to keep the cab warm in the winter and cool in the summer. Towers that offer the variety of services will typically drive across town from one job to the next, and will tend to use more fuel than those that wait for collisions.

While dedicated collision towers generally have more basic tow trucks designed to recover passenger vehicles from roadside accidents, more diversified towers will have a fleet of different vehicles to handle different jobs. Their basic tow trucks will also often have more equipment and be able to handle more varying jobs. Their heavier duty vehicles will also have greater fuel consumption.

As a result, while the tow operators conceded that 24,000 litres per year might be a relatively appropriate fuel consumption figure for dedicated collision towers, staff heard that the figure does not accurately reflect the fuel consumption of more diversified tow operators. Some of the operators present said they could provide average usage. Staff followed up with these operators but were unable to get any detailed information.

Insurance stakeholders believed that 24,000 litres of fuel per year is an over-estimate. At the same time, they posited that the high consumption of fuel for many tow trucks was due to idling while waiting for an accident.

Insurance stakeholders also believed that newer vehicles are materially more fuel efficient than in 2005 and that any calculation pertaining to fuel usage necessarily needs to take these improvements into account.

Neither the tow operators or other stakeholders disagreed with staff respecting the rate of increase for fuel prices (50.5%) for the period since the last increase.

Insurance

Tow operators agreed with the insurance premium number used by staff in their rate calculation.

Other stakeholders, and in particular those representing the insurance industry, believed that the average annual premium of \$11,500 quoted by tow truck operators is too high and likely represents the premium for operators with a driving record with convictions. Some of the insurance stakeholders volunteered to look into and provide more realistic premiums. Insurance stakeholders believed that insurance premiums should more likely represent approximately 4% of operating costs (as opposed to the proposed 13% calculated by staff, as per Table 1). Staff followed up with the insurance representatives,

but received premium quotes that were not specifically for tow trucks and did not meet the minimum coverage required in the By-law.

Vehicle Price

Tow trucks are expensive, custom-built vehicles. The truck is purchased separately from the hydraulic systems. Trucks may last beyond five years, but the hydraulic systems can last ten or more. As a result, hydraulic systems are often swapped into new vehicles. Tow operators stated that, depending on the system, hydraulics can represent almost half of the vehicle cost. There are only four major companies in the region that custom-build tow trucks.

Tow operators provided an estimated cost of \$126,500 for a new tow truck. In calculating the annual expense associated with this cost, staff assumed a four-year amortization at an 8% financing rate. Insurance stakeholders claimed that the price was inflated by as much as \$40,000 to \$50,000. Insurance industry stakeholders also questioned whether using a 4-year amortization for the vehicle was reflective of the actual life cycle of a tow truck. They believed that their useful life is longer and that the cost should be amortized over this longer period. This last point was generally corroborated by the tow industry.

Many tow trucks are now being leased. One of the tow operators indicated that lease payments for regular tow trucks tend to be \$1,800 - \$2,000 per month and have terms of five years.

Tow operators rejected staff's assertion that the cost of vehicles has fallen by 7.4% since 2005. This figure was obtained from Statistics Canada with respect to passenger vehicles. In the estimation of tow operators, tow truck prices have risen by 30% since 2005. Other stakeholders did not disagree with staff's conclusion that vehicle prices had fallen.

Maintenance

Maintenance refers to anything that has to be done to maintain the vehicle and its equipment road and job-worthy.

Tow operators generally did not have an issue with the maintenance number of \$8,200 used by staff. Their proposed number approximated \$9,000 per year and, according to them, included basic maintenance of the vehicles and equipment (i.e., did not include any major mechanical repair or equipment failure).

Other stakeholders expressed some concern over what specific items should be included as part of maintenance. They were concerned that a broader interpretation of maintenance could include related costs such as down-time (i.e., the opportunity cost of a tow truck being maintained). The current indexing model reflects the maintenance expenses provided by the tow industry, but it does not include down-time.

Both towers and other stakeholders did not have concerns with staff's conclusion that the costs associated with maintenance had increased by 16.2% between 2005 and 2011.

Other

There was a suggestion that the rate calculation should include staffing and overhead costs. Tow truck owners often pay drivers. In addition, there are office and other overhead costs that are a part of operating the business and should be considered.

Tow operators suggested that the accident tow business has very low margins and may even be a money-losing proposition. When asked why they continued to participate in this line of business, they answered that accident tows are part and parcel of broader contracts for other service providers (such as auto clubs).

Towers also expressed their frustration over the perception that people have about padded bills. They posited that final bills also include Collision Reporting Centre ("CRC") charges, storage fees, and repair costs.

When asked about the legitimacy of differential rates for accident tows from streets and highways, tow operators indicated that highway tows generally involved more safety-related measures and took longer. They also cited higher risk and believed that this should be captured in a differentiated rate.

When asked about the legitimacy of differential rates for accident tows from streets and highways, other stakeholders agreed that there is a difference that should be recognized in the rates. They said that highway tows involve greater risk to the tow operator.

Many tow operators at the consultation expressed their frustration over the low rates and the failure by the City to review rates in a timelier manner. A number of tow operators reiterated their position that Toronto should have a flat-rate of \$350. At the same time, they expressed their willingness to accept an interim increase of 21.6%, as per the October 2011 report, until a full review can be conducted.

Other stakeholders suggested that most GTA municipalities have accident tow rates that are too high and that Toronto should not be guided by rates there. They also said that the main reason bordering municipalities had a higher base rate in the past was the low population density, which created negative economies of scale for operators. They argued that the conditions in the GTA are very different now; as there are more people living in the bordering municipalities than in Toronto.

Although stakeholders said that the Toronto formula required refinement, they generally supported the more analytical approach taken by Toronto.

Finally, stakeholders expressed some concern about tow rates being reviewed outside of the broader tow truck industry review. They argued that the rates were connected to industry conditions and requirements, such as the required drop at the CRCs.

Staff Analysis, Conclusions and Recommendations

There are two main issues with respect to the setting of tow rates: the initial base rate and the indexing model by which to increase rates. The latter has been the foremost subject of discussion, but if the initial rate has not been reflective of the industry's costs, any rate indexing changes, whether appropriate or not, would further distort rates.

Staff have not been able to trace the origin of collision tow rates in the City. Through discussions with stakeholders, staff have been advised that many tow trucks operate as part of larger fleets and are involved in a mix of towing activities. Anecdotally, one operator indicated that collisions only made up some 5% of his company's business. The cost structure for such an operator would be vastly different than the cost structure for a single independent dedicated collision tower.

In addition, staff have found it very difficult to obtain valid (truly representative of what is being measured) and reliable (available and verifiable) data. Most of the information provided thus far, has come from the tow industry and relevant stakeholders and has been anecdotal. Although some have offered to provide data, none has yet come forward with information that can be verified. Much of the information required by City staff is seen as proprietary and competitively sensitive.

The indexing model developed by the City in 2006 and used to calculate the last rate increase approved by City Council used the main cost drivers outlined in Table 1, as identified by the industry at the time, to calculate the relative weights of each of the drivers. It also used verifiable price information to determine any rate changes.

In conclusion, staff conclude that more work needs to be carried out to determine an initial base rate. In addition, there has to be recognition of the fact that the cost structure of industry participants can vary significantly and therefore a rate that may be profitable for one type of operator could represent a financial loss to another. In addition, although the City needs to set rates that will promote a healthy, competitive industry, it also needs to protect the broader public interest and ensure that consumers are being treated fairly. In this respect, rates cannot be divorced from other regulatory provisions.

Although staff believe that its current indexing model is effective in determining rate increases, there is no existing foundational model to be used in the validation of the base rate. As a result, staff recommend that more work be carried out to develop a model that can be relied upon. In the meantime, staff are of the opinion that a modest increase is required, as there is little doubt that costs have risen, especially with respect to fuel, which has risen by more than 50% in the last six years. Staff therefore recommend that

rates be increased by an amount that equates to an average of the annual Toronto All-Items CPI for the period of 2005-2011. This increase amounts to 2.0% and will maintain Toronto's tow rates among the lowest in the GTA.

In the October 2011 report from the Acting Executive Director, staff had recommended that the highway and street accident tow rates be blended. The basis for the recommendation was that there seemed to be no quantifiable rationale for the difference in rates (as evidenced by the fact that no other municipality has such differential rates). In addition, staff believed that a single rate would eliminate the ambiguity as to when each rate applied (i.e., erroneously applying the highway rate on major roadways). As a result of the consultations, and the opinion of both towers and other stakeholders, staff are now recommending that street and highway accident tow rates not be harmonised in the interim, pending the comprehensive review. As such, staff recommend that the interim increase be applied to the street and highway rates separately.

Staff will continue its work on tow rates as part of its greater review and shall make specific recommendations as to what rates should be charged and how those rates should be calculated on a go-forward basis.

As part of its work, staff will consult with tow operators and other relevant stakeholders, such as insurance companies, auto service clubs, the CRC, and the general public. It is the intention of staff to develop a costing model for determining towing rates that takes into account both demand and supply factors, and which will provide for a healthy industry that encourages competition and responsible operation on the one hand and, at the same time, protects the interests of consumers on the other.

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