australian diagnostic imaging association

COMPETITIVE NEUTRALITY IN NSW: IPART NSW ISSUES PAPER

ADIA response, August 2022

ADIA is grateful for the opportunity to provide a response to IPART's issues paper on competitive neutrality in NSW.

We would welcome the opportunity to engage further with IPART NSW on this important issue. Please contact Chris Kane (CEO) via email [redacted]

About ADIA

ADIA is the peak body for radiology practices, representing over 750 clinics throughout Australia, both in the community and in private and public hospitals. ADIA promotes the ongoing development of policy, standards, and appropriate funding to ensure that all Australians have affordable access to quality radiology services. This supports radiology's central role in the diagnosis, treatment, and management of a broad range of conditions in every branch of medicine.

Competitive non-neutrality in the market for outpatient radiology services

ADIA produced the attached paper, *Bridging the gap: towards competitive neutrality in Medicare-funded radiology services*, in September 2021. The paper provides detail on a lack of competitive neutrality in the provision of radiology services in Australia. These issues are particularly prevalent in NSW.

In the case of public hospitals, radiology departments providing outpatient services are accessing funding twice: from public hospital funding (provided by the NSW Government), and from Medicare (provided by the Commonwealth Government). Private radiology providers competing in the same market, on the other hand, deliver the same service for a significantly smaller cost to government – the Medicare rebate alone.

Public hospital radiology departments are also competing in the market for services to workers compensation patients, pricing their services well below market rates because the costs for the service are already covered by hospital funding. This is dramatically distorting the market for those services.

Hospital funding covers most service costs

Public hospital radiology departments are funded by the NSW Government to provide radiology services to inpatients and outpatients. Costs covered by this funding include:

- Staff wages and on-costs, including radiologists and nuclear medicine specialists, technical staff including radiographers and sonographers, nurses, and administrative support;
- Equipment, including purchase of assets, installation, repairs and maintenance, and IT system costs;
- Utilities including electricity;
- Administrative costs; and

- Consumables, covering a host of items from eyewear, gloves and hand protection, to biopsy needles and ultrasound gel, to patient and radiation protection.

Public hospitals enjoy tax exemptions

Public hospitals enjoy several tax exemptions which are not available to private practices:

- Land tax is imposed on commercial property in NSW.[1] Therefore, private radiology practices pay land tax on premises they own, while public hospitals do not.

  While it is common for radiology providers to be tenants and therefore avoid land tax, it is likely that the rental payments reflect some of the land tax borne by the landlords, depending on vacancy rates and the ability of the tenant to vacate the premises.[2] However, radiology practices are not able to easily move premises due to the value, size, and specialist fittings of their equipment.

- Public hospitals are exempt from payroll tax. In private radiology, payroll tax is a significant cost, amounting to 4.85% above the eligible threshold in NSW.[3]

- Hospitals are exempt from fringe benefits tax (FBT), up to $17,000 per employee.[4] Some public hospitals use the FBT exemption to contribute to attractive salary packages to attract and retain staff.

- Public hospitals are exempt from income tax, an exemption that extends to radiology provided to private outpatients,[5] despite those Medicare-eligible services being provided using public hospital funding.

- Hospital employees can access to up to $5,000 per year in salary packaged 'meal entertainment', which can include meals, and associated accommodation and travel.[6]

These tax advantages amount to a substantial competitive advantage over the public hospitals' private competitors. In 2017, Verve Economics produced a submission to Treasury's Competitive Neutrality Review for ADIA, calculating that if the income tax exemption, payroll tax exemptions, FBT exemptions and entertainment cost exemptions were to apply to a private practice, they could

[1] NSW Government, The Treasury (2013) Interstate Comparison of Taxes 2015-16, Research & Information Paper trp 16-01, December, p.31. Available at: https://www.treasury.nsw.gov.au/sites/default/files/pdf/TRP16-01_Interstate_Comparison_of_Taxes_2015-16_-_pdf.pdf (Accessed 29/06/21)
[2] Access Economics (2007) Scope for differential private/public Medicare rebates for radiology services, Report prepared for ADIA.
[3] Payroll Tax Australia (last updated 11/07/22) Payroll tax rates and thresholds. Available at: https://www.payrolltax.gov.au/resources#resources__rates_and_thresholds (Accessed 22/76/21)
[4] Australian Government, Australian Taxation Office (last modified 09/05/22) Fringe benefits tax – Rates and thresholds. Available at: https://www.ato.gov.au/rates/fbt/ (Accessed 22/07/22)
[5] Verve Economics (2017) Competitive neutrality issues with provision of outpatient diagnostic imaging services in public hospitals: A submission to the Competitive Neutrality Review. Canberra, Verve Economics. Available at: https://www.adia.asn.au/public/3/files/ADIA%20Submission%20to%20Competitive%20Neutrality%20Review.pdf (Accessed 20/07/22)
[6] Australian Government, Australian Taxation Office (2019) Is the benefit exempt from FBT? Available at: https://www.ato.gov.au/general/fringe-benefits-tax-(fbt)/in-detail/non-profit-organisations/fbt-and-entertainment-for-non-profit-organisations/?page=6 (Accessed 22/07/22)

potentially enable the clinic to lower charges by up to 14% without affecting the after-tax return on capital achieved by the practice.[7]

Use of rights of private practice arrangements

Public hospitals access Medicare funding by having medical specialists (including radiologists) treat patients privately, including outpatients. These arrangements are known as Rights of Private Practice (RoPP).[8]

When utilising RoPP to provide services to outpatients, radiologists either:

- assign the Medicare benefit to the hospital, and receive an allowance; or
- retain all Medicare revenue generated but pay a facility charge and administrative fee to the hospital. Earnings may be capped at a specified level; or
- share in the Medicare revenue generated with the hospital.[9]

Public hospitals are not required to ensure that facility charges reflect the true value of facilities and services used by radiologists when they exercise their RoPP.

Evaluations of RoPP arrangements in Australian public hospitals have all questioned the adequacy of the fees that medical specialists are charged for the use of facilities, equipment and services when seeing private outpatients. For example, based on a 2008 audit of RoPP arrangements in Victoria the Victorian Auditor-General concluded:

> "...there was no evidence that the 'fee' paid by the medical specialists as part of the facility agreements for the use of facilities, staff and other services reflected the real value of public resources being used."[10]

This system enables radiologists in public hospitals to earn substantial incomes from outpatient work, which is not available to radiologists at private practices and generates a labour market advantage for public hospitals.

Question 1. What obligations should competitive neutrality policies place on government business activities?

Government business activities should be obliged to publish a true account of any benefits received (including funding and tax exemptions) for the provision of goods and services, in addition to the income earned from delivering those services.

Where income earned is at a cost to government (that is, government is the buyer of the goods or services, as in the case of public hospital radiology providers who bill outpatient services to Medicare), then the true cost to government can be determined by combining that income with the costs already met by government. Only then can the true cost of providing goods and services be properly understood, giving a realistic indication of the degree of competitive advantage enjoyed by government businesses.

[7] Verve Economics (2017) Op cit.
[8] Ibid.
[9] Ibid.
[10] Victorian Auditor-General (2008) Private Practice Arrangements in Health Services, Report 2008-09: 4, p. 23. Available at: https://www.audit.vic.gov.au/sites/default/files/20081029-Health-Services-Private-Practice-Arrangements.pdf (Accessed 30/06/2021)

Question 2. What guidance do government agencies require to support them to correctly apply competitive neutrality principles to their activities?

Required rate of return

The case studied cited in the *Issues paper* on page 22 (Box 3.4) showcases an example of a breach of competitive neutrality in the wider diagnostic imaging sector, specifically failure to achieve a commercial rate of return.

In the case described, PETNET Australia Pty Limited was a wholly owned subsidiary of the Commonwealth Government's Australian Nuclear Science and Technology Organisation (ANSTO). PETNET was not pricing to cover its costs, nor was it generating commercially acceptable profits in its manufacture of nuclear medicine radiopharmaceuticals.

The Australian Government Competitive Neutrality Complaints Office (CNCO) found that:

> "For ANSTO to comply with competitive neutrality policy, it would need to adjust PETNET Australia's business model such that it can be expected to achieve a commercial rate of return that reflects its risk profile and the full investment in PETNET Australia."[11]

In this instance, PETNET's pricing was competitive because it did not price at levels that appropriately factored in a commercial rate of return.

In the case of radiology, the 'sticker price' to the state/taxpayer of providing the services is the same as private providers – namely, the Medicare rebate. However, this does not factor in the other costs to provide the service, which are part of the overall costs (namely, grant funding, along with other benefits in kind and tax breaks). Any review of public hospital radiology rates of return (and indeed, for other industries) would need to factor in the *true cost* of providing the goods/services.

For this reason, in order to ensure competitive neutrality, consideration could be given to reducing the financial support provided to government owned businesses *or* reduce the reward on the point of providing the good or service (in radiology's case, the Medicare rebate).

Guidance should therefore be provided to enable government businesses to ensure that they have accounted for all means of financial support in determining a true cost of delivering goods and services, and accounting for a required rate of return on operations.

Question 3. How should governments identify the activities that need to apply competitive neutrality principles?

Government business activities

The Issues Paper notes that the application of competitive neutrality policies to government owned businesses requires consideration of whether or not the goods/services provided are classed as 'business activity'.

The NSW competitive neutrality policy goes on to define government businesses generally as organisational units which "are subject to Executive control."[12]

[11] Australian Government Competitive Neutrality Complaints Office (2012) PETNET Australia, Investigation No 15.

[12] NSW Treasury (2002), Policy Statement on the Application of Competitive Neutrality (TPP02-1), January 2002, p 3. Cited in IPART (2022) Competitive neutrality in NSW: Issues paper. Sydney, IPART, p. 36.

Some government enterprises may dispute the degree of "executive control" of their operations, which might be used to argue that they are excluded from 'government business' criteria in competitive neutrality tests.

However, in the case of NSW public hospital radiology departments, the government *does* exercise executive control because of its fiscal support and policy management.

Significant business activities

The significance test is of particular interest to ADIA, because most public hospital radiology departments undertake a relatively small level of activity (for example, it is unlikely that any single hospital would be generating more than $10 million in Medicare revenue from outpatient radiology services).

However, when these activities are aggregated, the market share of public hospitals in the outpatient radiology market is substantial, and has a significant impact on the operation of that market.

Accordingly, the significance test should be sufficiently flexible to enable activities by government business enterprises to be considered in aggregate. In the case of radiology, this would allow IPART to consider the outpatient services provided by all public hospital radiology departments in NSW in a competitive neutrality assessment.

The public interest test

The Issues paper notes that "Competitive neutrality principles only apply where there is a net public interest in applying them." (page 42).

ADIA previously received legal advice that despite the policy in place, the public interest test tends to be construed quite narrowly on most Australian jurisdictions. In the case of radiology, this means that the policy of public hospitals to bulk bill services to outpatients funded by Medicare would be considered in the public interest and would justify competitive non-neutrality.

This is despite many costs and adverse consequences associated with competitive non-neutrality in radiology:

- Public hospital radiology departments prioritising outpatients (who generate Medicare revenue) over hospital inpatients. The difference in waiting time can be several days or more. ADIA is aware of one Sydney public hospital which transports inpatients requiring MRI to another hospital in the network around 30 minutes away (which has a Medicare-ineligible MRI scanner), so that it can maximise the number of Medicare-funded outpatient examinations on its own Medicare-eligible MRI scanner.
- ADIA understands that at some public hospitals, reporting of inpatient examinations is performed primarily by registrars, to allow radiologists to focus on reporting outpatient examinations which generate Medicare revenue. It is entirely appropriate for registrars to report inpatient examinations, with input from radiologists as required. However, where allocation of work is determined by financial rather than clinical considerations, the risks to patient safety are increased.
- In some cases, routine inpatient examinations are not reported by radiologists at all, or are only reported after a long delay. This carries serious risks for patients.

- Public hospitals 'cherry pick' the services they provide, rather than offering a comprehensive range of services. For example, patients presenting to some public hospitals with a referral for low rebate items like obstetric ultrasound or mammography are told to attend a private practice instead; either because the hospital intentionally limits capacity with resulting waiting lists, or does not offer the service at all. This demonstrates that for some public hospitals, the overriding objective of providing outpatient services is revenue generation.
- Rights of private practice arrangements and tax exemptions distort the labour market for radiologists, increasing the wages and other benefits that private providers must offer to attract radiologists. Higher costs are ultimately passed on to patients.

The public interest test should be designed to enable consideration of all relevant factors in a cost-benefit analysis, so that all the implications above can be incorporated into the analysis.

Question 4. How often should government businesses re-assess their activities for competitive neutrality? Question 5. What circumstances could trigger a re-assessment?

ADIA suggests that government businesses re-assess their activities for competitive neutrality every five years, as this would take account of policy changes and developments that may impact on government business. In the case of radiology, the National Health Reform Agreement covers five-year periods, with the next agreement for 2025.

Specific circumstances that could trigger a re-assessment include:

- Government enacting executive powers to take control of a major government owned enterprise.
- Changes in policy and legislation that directly and significantly affect government businesses.

Question 6. What types of information should government businesses publish to demonstrate compliance with competitive neutrality policies and when? What types of information should not be published?

The Issues Paper notes that in its submission to the Harper Review, the Commonwealth Productivity Commission recommended that to improve transparency, government businesses should publish information about steps taken to comply with competitive neutrality policies.[13]

In order to comply with competitive neutrality polices, published information could include:

- Financial support received from government, including direct funding.
- Other support in-kind, including tax exemptions.
- Any income received from the provision of goods and services (such as Medicare rebates)

Publishing this information will demonstrate the true cost of government owned businesses providing goods and services.

[13] Harper, I, McCluskey, S and O'Bryan, M, *Competition Policy Review Final Report*, March 2015, p. 262. Cited in IPART (2022) Op cit.

Question 7. How can the processes for lodging or investigating complaints be improved?

ADIA's submission to the Competitive Neutrality Review (2017) noted that there is a surprising lack of complaints about public hospitals in the radiology sector, suggesting that the reason for the low number of complaints has been a belief that any determination will find that public benefit considerations will be found to outweigh cost considerations and the complaint will fail.[14]

Therefore, the concern for complainants is that, even in cases where there is clear evidence of breaches of competitive neutrality, a government business can argue that the value of its public benefit outweighs any costs of providing the good or service (see question 3 above).

The determination that a 'public benefit' exists that outweighs established breaches of competitive neutrality should be made solely by the independent regulator, IPART NSW, and any potentially affected non-government businesses should be invited to make submissions to any related investigation by IPART in order to improve the quality and accuracy of the ultimate determination.

ADIA suggests that the when designing a new process for lodging and investigating complaints, IPART should be cognisant of the issues described above, so that complainants can be confident that competitive neutrality concerns have a serious prospect of being addressed through the NSW competitive neutrality framework.

[14] Verve Economics (2017) Op cit. p. 4.