

06/144

Ms Hilary Metcalf
Director, Pathology Section
Diagnostics and Technology Branch
Department of Health and Ageing
MDP 107, GPO Box 9848
CANBERRA ACT 2601

Dear Ms Metcalf

Further to my correspondence of earlier this week I provide now the AMA's comments regarding the proposed leasing and valuation arrangements as raised in the discussion papers pertaining to the proposed secondary legislation to support the *Health Insurance Amendment (Inappropriate and Prohibited Practices and Other Measures) Act 2007*.

The AMA has significant concerns regarding the proposed arrangements and believes the Government would be wise to further consider the full impact that these arrangements will have on the medical profession and their patients.

The AMA welcomes the opportunity to further discuss these matters and to that end would welcome a meeting with the Department to assist the Government formulate the most appropriate way forward with this secondary legislation.

Yours sincerely

Warwick Hough
Senior Manager
General Practice, Legal Services and Workplace Policy Section
February 2007

AMA Submission Paper re Prohibited Pathology and Diagnostic Imaging Practices

Part 2 Market Value and Leasing Arrangements

There is no evidence that there has been widespread abuse of the current arrangements resulting in excess cost to the Government/taxpayer. This is because doctors act ethically and in the best interests of their patient. The proposed secondary legislation will only add costs to the system for everyone involved from the Government through to the patient. Regulatory and compliance costs are inflationary and, have no doubt, will ultimately impact on patient service costs.

The AMA is concerned that the proposed principles will potentially interfere with legitimate commercial arrangements. The amendments to the Health Insurance Act are concerned with preventing inappropriate behaviour. However, the test of market value proposed relies on the principles outlined in *Spencer v. The Commonwealth* (1907) – which concerned the compulsory acquisition of land. We do not think this test in *Spencer* can be reasonably applied in these circumstances.

Courts have long recognised the difficulty in assessing what is commercially realistic and a cautious approach should be adopted. The Department should look at the purpose of the arrangement to determine whether or not it is inappropriate.

The Department must take into account a key principle established by the Courts - that an arrangement should not be brought into question simply because of an assessment of how much an entity ought to spend.

The AMA believes that the Government should adopt a test that is similar to that set out in *Federal Commissioner of Taxation v Phillips* (78 ATC 4261) (“*Phillips*”). While this case essentially dealt with taxation law, it did deal with what should be regarded as a legitimate business arrangement. In particular, the Court decided that the purpose of an arrangement could only be brought into question if an expenditure was found to be grossly excessive.

This approach should guide the construction of any regulations. Narrow guidelines with limited latitude will interfere with perfectly legitimate behaviour. Proposed regulations should seek to capture those arrangements that are a clear departure from normal market practices.

The proposed criteria for determining market value does not recognise reasonable business practice and does not recognise developments in the legal concept of market value. The Department is intent on excluding any special value to either party from the definition of market value.

This approach is out of date according to Professor Bernard Marks, Adjunct Professor of Law at Bond University who in a 1996 paper titled “Valuation Principles in the Income Tax Assessment Act” at page 160 states

It is submitted that, on proper consideration, an Australian court would both quickly and decisively recognise, as did Scott LJ in the Court of Appeal in *Robinson Bros (Brewers) Limited*, that the exclusion of special value from market value in the hypothetical market test was an 'economic paradox' and a 'contradiction in terms '.

Professor Marks highlights that special value is now widely recognised in other jurisdictions highlighting in the same paper at page 140 that:

Since 1938, market rent has been assessed in the United Kingdom on the basis that all special value to a special tenant is included in market value. Indeed, the courts have gone further by holding that, in determining the additional market rental value of a property to a possible tenant because of its special adaptability or use to him

It is reasonable to allow valuations based on best use of the premises and the capacity of the purchaser to pay. To remove relevant factors in determining a fair price such as the proximity of one medical service provider to another is to ignore the true market value.

With regard to providers leasing from requesters, or vice versa, the AMA is of the view that a simple clause in leasing contracts clearly stating and agreed to by both parties that the requester is under no obligation as part of the lease arrangement to refer services to the provider should prevent any consideration that an inducement has been provided.

It is a reality that pathology and diagnostic imaging providers desire premises located in the proximity of other medical professionals just as it is a reality that businesses dependent on passing trade prefer and pay a premium for locations where there is high foot traffic. Providers are conscious of the reality that patients like convenience and co-locating premises is perfectly rational behaviour.

To deny this reality when determining the market value is to abandon normal commercial principles and results in a price that is less than the true market value.

Rental prices are also determined by multiple factors. These may include age of building, existing fixtures, floor space, location of the space, use of the space, expected business turnover, not to mention all the relevant factors that the Government is trying to exclude when determining a value. When obtaining valuations for leases or rentals it would be unreasonable to base a valuation on leasing or renting the same space to anyone but a like business.

For example if a general practice owned a building and was leasing space to specialists, a pathology provider, allied health professionals and a café, it is to be expected that they would all be paying a different price per square metre based on their location within the building, the use of the space, expected turnover and thus their capacity to pay.

The Government should be encouraging investment in medical infrastructure. It should ensure that the environment supports general practice in its efforts to train medical students and new GPs, and supports retention of the GP workforce. The current proposals have the very real potential to discourage GPs from investing further in their practices and limit patient access to a convenient range of services.

The AMA believes the Government is being overly restrictive with regard to leasing arrangements and it seems extremely unfair that medical providers are faced with such levels of scrutiny compared to other market arrangements where location, proximity to trade and capacity to pay is always a factor in determining a fair price.

Furthermore, determining the market value to be the average of two valuations is an arbitrary approach that does not recognise that valuation is not an exact science. Why should a business be forced to take an average? Rational behaviour dictates that business will pursue the valuation that is most favourable.

It is perfectly rational economic behaviour to expect that the assessed market value would be the floor price from which any landlord would be aiming to improve upon. They would want to seek the best deal possible and the AMA sees no reason as to why they should be restricted to demanding no more than 10% above this figure.

The proposed variation of 10% from market value is inappropriate especially when considering the proposed test of market value – which wrongly excludes special factors. The Courts have allowed far more latitude when assessing variations in property value.

Research into the legal context of property valuation variations (the margin of error) indicate that judges have allowed up to $\pm 20\%$ following expert evidence from valuers and for commercial properties it is expected that realistic range for variation between valuations is $\pm 5-30\%$ ¹.

In relation to a single valuation obtained by Medicare Australia, there is no information provided on whether this can be challenged. Parties should have the right to challenge such a valuation within a defined period.

When considering cases where the rent is lower than market value, relevant circumstances such as workplace shortages need to be taken into account. For example a practice in an outer metropolitan area may reasonably provide a room to a visiting diagnostic imaging professional at a nominal fee in order to encourage their attendance at the practice.

The proposed guidelines will discourage the co-location of medical services with pathology or diagnostic imaging services. In addition, the AMA is concerned that requesters leasing space to providers will be driven into accepting less than they could reasonably expect to receive so as to avoid any potential breach of the Health Insurance Act and the resulting possibility of legal action.

This would simply deliver a windfall gain to providers. The Department needs to revisit the intent of the original legislation. Proposed regulations should focus on detecting inappropriate behaviour and not some arbitrary assessment of what is commercial versus what is not commercial.

¹ Skitmore, Martin and Irons, Janine and Armitage, Lynne (2007) Valuation accuracy and variation: a meta analysis. In proceedings 13th Pacific Rim Real Estate Society Conference, Fremantle, WA.