

# Royal Flying Doctor Service of Australia - Submission to Productivity Commission

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## 1 Executive summary

### 1.1 Summary

This submission responds to some of the issues raised in the Productivity Commission Issues Paper on the Contribution of the Not for Profit Sector (“**NFP Issues Paper**”).

The key points of this submission are:

#### **Recommendations not taken up from previous inquiries**

- (a) The RFDS supports the introduction of uniform fundraising legislation. A National Fundraising Act including the minimum features recommended by the Senate Inquiry into disclosure regimes for charities and not for profits would significantly reduce the time and resources (and therefore costs) to NFPs in complying with fundraising regulation.

#### **Attracting paid and volunteer workers**

- (b) The RFDS incurs substantial difficulties and expense in attracting and retaining paid and volunteer workers in rural and remote Australian communities. The RFDS relies on the benefits it receives as an NFP to avoid being placed in a position of relative disadvantage compared to profit-driven organisations operating from central locations.
- (c) NFPs are disadvantaged in comparison with for-profit firms in respect of providing housing assistance for employees in remote locations, which is one of the key ways to attract personnel to provide services in remote communities.

#### **Factors impeding and facilitating the spread of knowledge**

- (d) Several factors impede the spread of knowledge between NFPs including the diversity of the areas in which they operate and the sensitivity of the knowledge they retain. However, unfortunately these are not necessarily factors that can be addressed or removed.

#### **Trends in government funded services**

- (e) We provide comment on RFDS’s experience in respect of trends in government funded services and submit that NFPs are often able to provide community services effectively and efficiently in circumstances where government provided services have previously been ineffective.

#### **Competitive neutrality**

- (f) There is significant and persuasive evidence to show that there is no real competitive neutrality issue arising from the more limited tax concessions received by NFPs in relation to their commercial operations. It is submitted that removing these tax concessions would have minimal

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impact on government revenue yet the potential to significantly impact upon NFPs and the services they provide.

- (g) The commercial operations of NFPs can be divided into two categories. The first describes commercial operations which are consistent with the charitable activities of the NFP. The RFDS falls within this category. The second category describes commercial operations which are unrelated to the core business of the NFP but whose profits are directed back to the NFP. An understanding of this distinction explains why some businesses perceive that NFPs obtain a competitive advantage.
- (h) The RFDS's experience in competing against profit-driven organisations is very much one of a level playing field. The RFDS operates along similar lines to for-profit organisations by practicing good governance, maintaining payroll records and conducting annual audits. This level playing field is also ensured by other regulatory and external government requirements that apply when tendering for government contracts.

#### **Effect of government funding on other services provided by NFPs**

- (i) We outline the integrated nature of the services the RFDS provides, and the economies of scale generated, and government funding is an important part of this.

#### **Arrangements which promote efficiencies and effectiveness**

- (j) The RFDS submits that NFPs should be actively encouraged to prioritise good governance strategies.
- (k) The recent trend towards shorter term contracts for services put to tender may result in increased overall costs due to the costs associated with transitioning between providers and the start-up costs of new service providers, if they are unable to be amortised over an appropriate period.
- (l) The reporting requirements that apply in respect of NFPs are inconsistent and confusing, and vary greatly between government departments and agencies. The RFDS suggests that greater consistency in government reporting requirements would lead to greater efficiency and reduce costs in the sector.

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## **2 Background**

### **2.1 RFDS**

The RFDS is a not-for-profit organisation (“NFP”) which provides emergency aeromedical evacuation services and health clinics in rural and remote Australia, as well as inter-hospital air ambulance services between medical facilities around Australia.

The RFDS is made up of seven entities, comprising six Operating Sections and the Australian Council, which is the national body. The Australian Council holds the funding agreement with the Commonwealth, and manages and distributes Commonwealth Government funds to each of the Operating Sections. It also coordinates national strategies. The Operating Sections are the operational bodies which own the aircraft and bases, and employ the pilots for the service.

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They also hold the funding agreements with the various State and Territory governments.

Further information about the RFDS is available on our website:  
<http://www.flyingdoctor.net/>.

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### 3 Scope of the study

#### 3.1 Recommendations not taken up from previous inquiries

The Commission has provided:

*Comments are invited on whether the findings and recommendations of previous inquiries remain relevant to the operations of the not for profit sector. Of those that continue to be relevant, and have not been acted on by government, which are the most important for improving the efficiency and effectiveness of the sector?*

The RFDS believes there is one recommendation that has not been acted on or fully implemented, but which is most important for improving the efficiency and effectiveness of the sector. Namely uniform national fundraising legislation.

#### 3.2 Uniform national fundraising legislation<sup>1</sup>

- (a) The RFDS submits that the introduction of uniform national fundraising legislation would increase the efficiency and effectiveness of the NFP sector. Currently, NFPs expend time and resources understanding and complying with the complex and different fundraising legislation in each State and Territory, and overlapping obligations under fundraising legislation and other regulatory requirements (such as, tax legislation).
- (b) A National Fundraising Act including the minimum features recommended by the Senate Inquiry into disclosure regimes for charities and not for profits (**2008 Senate Inquiry**), would significantly reduce the time and resources (and therefore costs) to NFPs in complying with fundraising regulation.

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<sup>1</sup> Recommendation no. 18, *Government response to Inquiry into Charitable Organisations in Australia (1995)*; and Recommendation no. 9, *Recommendations from the Senate Inquiry into disclosure regimes for charities and not for profit organisations*

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## 4 Enhancing the efficiency and effectiveness of the not for profit sector

### 4.1 Attracting paid and volunteer workers

The Commission has provided:

*Not for profit organisations are invited to comment on their experiences with attracting both paid and volunteer workers with the appropriate level of skills.*

*Comments are also invited on the extent to which regulations surrounding the use of paid and volunteer labour adversely affect the capabilities of not for profit organisations to undertake their activities. Where adverse effects occur, how might these be overcome?*

#### (a) RFDS's experience in attracting paid and volunteer workers

The RFDS draws strongly on both volunteer and paid staff to operate. Each Board of Directors is comprised solely of persons who volunteer their time. These include persons who are well known to the community, as well as business leaders, professionals, medical and aviation persons, all of whom devote their time and efforts because of their belief in the objects of the organisation and the difference that the RFDS can make to Australian society.

At the National level, former Governor General, Major General Michael Jeffery AC AO (Mil) CVO MC (Retd) has assumed the role of National Chair, taking over this role from the Hon Tim Fischer AC.

All directors are subject to the same legal requirements and responsibilities that apply to a for profit organisation.

Management staff are paid staff and the RFDS seeks to employ the right people for the role, applying proper selection processes.

Volunteers also form a key part of the fund raising support team, who collectively in the communities spread across Australia undertake the activities that generate donations to allow the RFDS to undertake its work.

The RFDS relies on all of those components.

Normal employment work place health and safety requirements apply to each of those levels and as a medical service provider the RFDS totally supports this degree of regulation to protect the health and safety of all whether they are paid or volunteer.

An increasing number of large businesses are including volunteer days for their staff, increasing the opportunity for those staff to provide free time to NFPs.

#### (i) Salaries offered to paid workers

The NFP sector cannot afford the salaries available in the for-profit sector, as the imperative is to minimise costs and maximise the amount spent on charitable activities. Whilst the profit-driven sector similarly seeks to minimise staffing costs, the NFP sector is at a particular disadvantage. Goods and services provided by the NFP sector are often provided at no cost, or where those services

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are government funded services, they are provided at a rate substantially below market value (as they would be if the government was providing them). Whilst this is of substantial benefit to the user and community, the trade-off is that limited funds are available to offer attractive salaries to prospective employees.

The RFDS employs around 800 staff nation-wide, and is highly dependent on use of the FBT concessions to attract and retain expert staff. Any reduction in the FBT concession would significantly affect the RFDS, would require us to pay considerably higher salaries to compete with the for-profit sector, and would have a direct impact on the scope of the services provided by the RFDS. Any reduction in the concession would translate directly into higher payroll costs, risking a reduction in our service, which would be counter-productive and of no benefit for the public health system.

In addition, the RFDS submits that the FBT exemption should not be replaced by an FBT rebate. Doing so would substantially increase administration and compliance costs for NFPs and have a detrimental impact on the RFDS's income flows.

(ii) Attracting employees to remote locations

The RFDS is in a unique position in that it operates in areas of Australia which would not otherwise receive emergency medical services.

The RFDS provides services from a number of bases, many of which are located in regional and remote parts of Australia, including Broken Hill, Dubbo, Charleville, Mt Isa, Alice Springs, Port Headland, Meekatharra, Kalgoorlie and Derby. It is often difficult for the RFDS to attract and retain medical, aviation and management staff in these areas.

The RFDS has gone to significant expense and effort to implement strategies to attract and retain staff. For example, some RFDS clinics operate out of central locations (such as Cairns) whilst servicing remote areas (such as Cape York and communities in Northern Queensland). Also, the RFDS actively seeks to distinguish itself from profit-based employers by offering unique and attractive employment opportunities. In respect of aviation, for example, the RFDS offers quality training and accreditation for pilots and has implemented a best-practice program to prevent pilot-fatigue. This innovative program has since been adopted by firms in the for-profit sector.

As demonstrated above, the RFDS incurs substantial difficulties and expense in servicing rural and remote Australian communities. Accordingly, any reduction in NFP benefits would place the RFDS (and comparable NFPs) in a position of relative disadvantage compared to profit-driven companies who enjoy the economic and human resources benefits of operating from a central location.

**(b) Effect of regulations around paid and volunteer workers on RFDS ability to undertake its activities**

A key difficulty associated with attracting and retaining employees in remote areas is providing those employees with adequate housing. Particularly where highly trained individuals, who are not necessarily available in the local area, are required for the services (such as pilots and medical personnel).

While for-profit companies operating in remote areas such as mining companies are generally prepared to purchase houses for their employees, NFPs (even if

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they have the financial resources) will generally consider that it is not appropriate to do so.

The alternative is for employees to receive fringe benefits in the form of rental or loan assistance in respect of housing. However, this is discouraged by the operation of the FBT exemption which only exempts such benefits to a cap of 50% of their value. Accordingly, the NFP sector is at a disadvantage when seeking to attract personnel to rural and remote areas.

**(c) Suggestions to overcome adverse effects**

The FBT exemption is extremely valuable to NFP organisations and should (at the very least) be retained in its current form. In addition, the RFDS recognises that the FBT exemption cap has remained unchanged for a long period of time and this has gradually eroded its value. Ideally, the FBT exemption cap should be increased to offset this erosion.

The RFDS also submits that the 50% cap on the FBT exemption for housing assistance be increased to reflect the difficulties that NFPs face in respect of housing in remote communities, perhaps in respect of a limited class of highly trained personnel such as emergency services.

**4.2 Factors impeding the spread of knowledge**

The Commission has provided:

*Comments are invited on what factors are impeding the spread of knowledge among Australian not for profit organisations regarding how well they deliver their outcomes and key drivers of their efficiency and effectiveness in doing so. Similarly, the Commission invites comment on what factors facilitate the spread of such knowledge and how these might be enhanced.*

The RFDS agrees with the Commission's comments that sharing knowledge between NFPs is an important mechanism to improving effectiveness and efficiency. Due to the unique drivers of NFPs, the nature of the services they provide and the areas of the community that they assist, NFPs often have innovative approaches to delivering services and assistance which may be relevant to NFPs in similar circumstances. NFPs are also generally eager to use government, business or academic research or assistance to inform and improve their methods of delivery. However, NFPs do not always have the time and money to devote to sharing this knowledge or accessing these resources.

**(a) Factors impeding the spread of knowledge between NFPs**

The RFDS co-operates and shares knowledge with other NFPs in various areas of our business, such as donor management.

However, there are several factors which impede collaboration and the spreading of knowledge between NFPs. For example:

- (i) the NFP sector is extremely large and encompasses a variety of organisations operating in distinct fields. As such, the knowledge and expertise gained by NFPs such as the Red Cross or Diabetes Australia will be fundamentally different and possibly of limited use to the RFDS (and vice versa);

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- (ii) the information retained is often sensitive to the operation of the NFP. In one sense, NFPs are in competition with other NFPs to secure limited donor funds. As such, some NFPs may be reluctant to share information which may jeopardise any competitive advantage they hold.

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## 5 Service delivery

### 5.1 Trends in government funded services

The Commission has provided:

*Comments are invited on trends in government funded services, including the extent to which governments are funding the traditional activities or new service initiatives of the not for profit sector and the extent to which governments are 'outsourcing' service provision to the not for profit sector.*

The RFDS submits that NFPs which receive government funding can be distinguished as follows:

- (a) “**government funded**” organisations - these receive 100% of their funding from government and are in effect, government bodies; and
- (b) “**government supported**” organisations - these have their income supplemented by government funding yet also receive income from other sources. The RFDS falls within this second category.

The operations of the RFDS are funded in part by:

- (a) Commonwealth funding for rural and remote services;
- (b) State/Territory funding for inter hospital patient transport services and air ambulance services;
- (c) Commonwealth and State and Territory funding for specific health programs or projects; and
- (d) public fundraising.

Some of the State and Territory services are tendered for commercially, in competition with private operators. The remainder of our services are not provided in competition with private operators, and there is probably no private organisation that could provide the same coverage as the RFDS in the remote areas. The RFDS submits that it would not be viable for a service provider operating on a purely commercial basis to provide emergency medical services to remote Australian communities.

The RFDS agrees with the Commission that the role of NFPs in providing welfare services should be central to the definition of government-funded services. Increasingly, NFPs are undertaking roles and providing services which were traditionally undertaken or provided by government. Particularly in the welfare areas, including health, employment and community services.

As the Commission acknowledges, there are certain advantages with having an NFP undertake roles or provide services, including NFPs having a more positive public image, NFPs being able to offer additional client services, and the ability

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for NFPs to access volunteer labour, dedicated staff and to enjoy funding support from other parts of the community rather than rely solely on government funding.

The RFDS provides emergency aeromedical evacuation services and healthcare clinics in rural and remote areas, and inter-hospital air ambulance services, across the country. The RFDS also undertakes specific health programs and projects, many of which are focused on primary health care initiatives. For example, in Queensland there are currently twenty three specific health projects including women's health, mental health in the bush, and other associated primary health initiatives.

Often, NFPs (such as the RFDS) are able to deliver services more effectively than their government counterparts. For example, Queensland Health constructed new hospital facilities in Cape York, yet was unable to source sufficient medical staff who were prepared to work there. This was partly due to the strained relationship between government and the community. However, the RFDS has been able to employ doctors at the Cairns base who are rostered to visit and stay at these Cape York hospitals and provide medical services. These doctors have been welcomed into the community and this arrangement has operated successfully for a number of years. This arrangement illustrates the high level of community respect for NFPs such as the RFDS and also shows how NFPs may be able to provide replacement services where the government service has been ineffective.

## 5.2 Competitive neutrality

The Commission has provided:

*Comments are also invited on experiences in relation to the relative treatment of for-profit and not-for-profit providers in competing for government contracts. Do arrangements at the Commonwealth and State/Territory levels provide competitive neutrality? If not, what features result in unequal treatment and how could this be addressed?*

In commenting on these issues, it is worthwhile setting out the issue of competitive neutrality in the context it generally is raised in relation to NFPs.

### (a) The competitive neutrality issue

Competitive neutrality is an issue that has been raised over the years in relation to NFPs engaging in 'commercial activities'. From time to time, for profit organisations argue that they are disadvantaged when compared against NFP's and that the principles of competitive neutrality should apply to NFPs.

Competitive neutrality was originally a concept most relevant to government, and arose as a result of a perceived need to create a level playing field in relation to the participation of government businesses in contestable environments. Governments enjoy a significant number of potential advantages over private sector competitors including exemptions from taxes, cheaper debt financing, absence of any requirement to make a commercial rate of return on assets or equity invested, exemption from some regulatory constraints or costs, and a reduced level of financial reporting. In order to offset these potential advantages, the Commonwealth government introduced a policy on competitive neutrality to:

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- (i) ensure that significant government business activities do not enjoy net competitive advantages over their for profit competitors simply by virtue of public ownership;
- (ii) eliminate potential resource allocation distortions arising from the public ownership of significant business activities operating in contestable environments; and
- (iii) to encourage fair and effective competition.

This policy only applies to significant business activities of agencies, and does not apply to non-business, non-profit activities.<sup>2</sup> Similarly, proponents of the competitive neutrality argument only take issue with the profit-based operations of NFPs. However, we suggest that the distinction between profit-based and non-commercial (or perceivably “charitable”) operations is not easily made. For example, it is incorrect to characterise a flight to a regional centre as generating “profit” for the RFDS and a flight to a remote community as resulting in “loss”. This is because each flight is dependent upon RFDS infrastructure and overheads which are funded by both government funding and the public contributions. Any attempt to distinguish the operations of the RFDS in this way would require fundamental organisational change and undermine our ability to provide emergency services regardless of geographical location.

A separation between commercial and non-commercial activities would also seriously compromise the efficiencies we have developed at a national level in our operations across the country. These are efficiencies that are requirements of our Commonwealth, State and Territory government contracts and have in part been the result of ongoing dialogue with government about the appropriate structure and operations of the RFDS. To change this now would, we submit, be a significant retrograde step and be contrary to principles of good governance and economic policy.

The RFDS submits that NFPs do not enjoy the same potential advantages over for-profit organisations as a government business, and not all NFPs enjoy tax concessions. However, proponents of the argument that principles of competitive neutrality should be applied to NFP organisations, will argue that to ensure competitive neutrality between NFPs and for profits, NFPs should have any concessional taxation treatment removed for their commercial operations. In particular, that income from commercial operations should be subject to income tax and that fringe benefits tax exemptions be removed.

**(b) Is there in fact a competitive neutrality issue?**

RFDS believes that there is significant and persuasive evidence to show that:

- (i) that there is no real competitive neutrality issue arising from the more limited tax concessions received by NFPs in relation to their commercial operations; and
- (ii) to remove these tax concessions would, based on experiences overseas, result in significantly greater compliance costs for NFPs and no real increase in government revenue, and consequently result in a reduction in funding available to NFPs to apply to the objects of their cause.

<sup>2</sup> Finance Circular No. 2004/01 and *Australian Government Competitive Neutrality Guidelines for Managers* February 2004 (Financial Management Guidance No.9).

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The “competitive neutrality” argument has been scrutinised and dismissed by a number of previous inquiries, as demonstrated below. Accordingly, the RFDS submits that it is unnecessary and of limited benefit to return to this issue.

In the context of the income tax exemption, the 1995 Industry Commission Report *Charitable Organisations in Australia* (“**the 1995 Report**”) clearly stated that the “income tax exemption does not compromise competitive neutrality between organisations.” This conclusion recognised in the *Inquiry into the Definition of Charities and Related Organisations*, 2001 (“**the 2001 Report**”). The 1995 Report suggested that the income tax exemption did not compromise competitive neutrality because the payment (or non-payment) of “after-profit” taxes “should not affect the behaviour of an organisation when deciding how to set its prices and how to minimise its costs.”<sup>3</sup> This is because all organisations make business decisions which aim to maximise profit and minimise costs, regardless of their taxation status.

In addition, the 1995 Report acknowledged that whilst NFPs receive certain advantages (such as cash flow), profit driven organisations also receive advantages (such as easier access to capital). Significantly, the 1995 Report concluded that “the overall situation is unclear” and did not propose any changes<sup>4</sup>. This suggests that for profit organisations are not disadvantaged, and, we submit, the competitive neutrality argument has no merit. The Inquiry also noted that, since the 1995 Report, other tax concessions available to not-for-profit organisations have been considerably reduced. In particular:

- (iii) the abolition of sales tax and its replacement with the GST (the GST exemption is only available for supplies not provided commercially); and
- (iv) various limitations that have since been imposed on FBT concessions.

There has also been a substantial body of international economic research showing that NFP market participation does not inevitably create an unlevel playing field. Namely that:

- (v) NFPs do not enjoy an unfair advantage over for profit competitors because of tax concessions. An NFP is unlikely to underprice its for profit competitor or accept a lower return on its investments due to any tax concessions; and
- (vi) tax concessions do not distort market competition because all organisations, regardless of their tax status, aim at maximising profits.<sup>5</sup>

Therefore, the RFDS believes there is no real competitive neutrality issue which private organisations claim arises because of the current tax concessions enjoyed by NFPs. Indeed, there is evidence based on the experience of the United Kingdom and the United States (both of which levy income tax on the commercial arm of charitable bodies) that the introduction of income tax on NFPs commercial activities would result in significantly greater compliance costs

<sup>3</sup> 1995 Report at XXXI.

<sup>4</sup> 1995 Report at XXXII.

<sup>5</sup> Dalton, Bronwen and Casey, John, Innovation or ill-gotten gains? Interpretations of nonprofit business venturing in Australia, the United Kingdom and the United States, Paper given at the ANZTSR Eighth Biennial Conference, pp24-26.

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for NFPs and no real increase in government revenue.<sup>6</sup> Greater compliance costs and any tax paid will only result in a reduction in funding going to the NFPs relevant cause (and would significantly impact smaller NFPs). This was also acknowledged by the 1995 Report.

If the income tax exemption is to be treated as some form of impediment to competitive neutrality then a company with substantial income tax losses could also be regarded as having some form of advantage.

The RFDS believes that the Australian income tax legislation does already contain some restrictions that could be argued as assisting with providing an equalisation between NFPs and for-profit entities. Division 250 of the *Income Tax Assessment Act 1997* (Cwlth) restricts the depreciation deductions available to for profit financiers and suppliers of depreciable assets where those assets are used by entities that are income tax exempt.

The effect of these provisions is to raise the effective cost of the finance to the NFP with the object of the similar outcome whether the NFP acquired the asset (and did not obtain an income tax deduction) or whether the financier as a for profit enterprise acquired the asset and leased it to the NFP.

Division 250 ensures competitive neutrality in respect of assets acquired and financed where those assets are used by a tax exempt NFP.

In considering the question of competitive neutrality, other issues of a broader nature need to be considered in any comparison between NFPs and other business structures.

**(c) Different types of “commercial operations” undertaken by NFPs**

It is also worthwhile noting that the term “commercial operations” is one that requires careful definition. The extent and manner in which NFP organisations engage in commercial operations vary enormously, and there are perhaps as many variations on the theme as there are not-for-profit organisations.

Governments at both State and Commonwealth levels regularly require arrangements with service providers including the RFDS to enter into contractual arrangements. These are often offered as a tender process in which both an NFP and a traditional business can compete. The services provided under this contract will be consistent with those provided by the NFP as part of its charitable activities. The funds received under these contracts may be likened to a contribution to costs.

This style of commercial operation can be distinguished from the situation where a business providing different services or goods to those that form part of the activities of the NFP is owned by the NFP, and the proceeds / profits that the business generates are used by the NFP to further its objects. It is in relation to this latter type of commercial operations that much of the concern about a lack of competitive neutrality arises.

The RFDS “commercial operations” are the first category, namely on a similar type to those provided to the community at no charge, albeit with support from Government and the public.

<sup>6</sup> Dalton, Bronwen and Casey, John, Innovation or ill-gotten gains? Interpretations of nonprofit business venturing in Australia, the United Kingdom and the United States, Paper given at the ANZTSR Eighth Biennial Conference, pp8-11.

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To conclude that all NFPs are obtaining an advantage (or even an unfair advantage) over their for-profit competitors is a significant over-simplification, and ignores the vast diversity of the sector. In relation to its operations, the RFDS disagrees that NFP organisations which undertake activities that are similar to their regular charitable activities enjoy an unfair advantage over for-profit organisations in this way, and suggests that imposing tax on commercial operations would only reduce the funding available for charitable activities and increase the reliance of the NFP sector on government funding.

This seems counter to government policy in recent years, of seeking to reduce the extent to which NFP organisations are reliant on government funding, and to have a strong NFP sector that has developed a number of different sources of income.

If there is a concern that there is inappropriate competitive behaviour, or unfair advantage, in some parts of the NFP sector, we suggest that should be addressed by the introduction of greater transparency and accountability in commercial activities, not by the removal of tax concessions. Competition law will also provide a framework for activities undertaken.

There are a range of other reasons for not taxing the commercial activities of NFP organisations, which include that charities are unable to raise equity or debt in capital markets unlike their for-profit competitors. This is partly because NFPs cannot appeal to their shareholders to raise funds. Instead, NFPs can undertake capital works and support longer term commitments by generating surplus funds from grants, donations and net income from commercial activities. Accordingly, commercial activities are an important source of funding for longer-term planning by NFPs and increasing the size and scale of their charitable activities. This was acknowledged in the 2001 Report<sup>7</sup>.

**(d) RFDS's experience in competing for government contracts**

The RFDS's experience of the relative treatment of NFPs and for-profit organisations has been very much one of a level playing field. The RFDS operates along very similar lines in terms of governance standards, application of business concepts and principles in conducting its operations to reflect a normal commercial basis used by a for-profit organisation in the search for the most efficient method of operation. For example, the RFDS has established key management structures, formal board governance standards, compiles annual audited reports, maintains payroll records no different to any other enterprise and maintains the strict documentation requirements applicable to the medical profession and to the aviation industry.

As outlined above, the Royal Flying Doctor Service provides emergency aeromedical evacuation services and healthcare clinics in rural and remote areas, and inter-hospital air ambulance services, across the country. Our operations are funded in part by:

- (i) Commonwealth funding for rural and remote services;
- (ii) State/Territory funding for air ambulance services; and
- (iii) public fundraising.

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<sup>7</sup> 1995 Report at XXXI-XXXII.

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Some of the State and Territory services are tendered for commercially, in competition with private operators. The remainder of our services are not provided in competition with private operators, and there is probably no private organisation that could provide the same coverage as the RFDS in the remote areas.

All activities within the broader RFDS organisation are conducted in a business style. A term that has been used to describe participants in the NFP sector is that it should be described as a Not for Loss Sector. That is the NFP organisation sets its budgets and direction each year with the goal that it will finish the year with a surplus of income over expenditure. This surplus is essential if the NFP is to be able to acquire additional assets for use in its activities and to fund the continued expansion and provision of services.

The RFDS's commercial operations are conducted on a commercial basis, and it tenders a commercial price and margin, as it believes that it needs to make a commercial return to properly price the risk of these operations. In New South Wales and Victoria, there is no cross-subsidisation between this and the other parts of the organisation, and the aircraft, pilots and other personnel and infrastructure required are sourced under separate arrangements from the rest of our activities. The RFDS's operations in Queensland have also started to move in this direction, and we suspect this will be the trend for the rest of the organisation in the coming years.

**(e) Do arrangements at the Commonwealth and State/Territory levels provide competitive neutrality?**

To respond to this issue, the RFDS believes it is necessary to look at:

- (i) whether there is a competitive neutrality issue arising independently from regulatory (ie tax) concessions;
- (ii) the arrangements around tendering for government contracts; and
- (iii) other regulatory and external government arrangements placed on NFPs.

As discussed above, the regulatory concessions that NFPs enjoy (ie tax concessions) do not themselves create a competitive neutrality issue when NFPs and for-profit organisations compete for government contracts.

In the RFDS's experience, tendering for contracts for the government funded services it provides, the RFDS competes on a level playing field with its for-profit competitors. The RFDS tenders for these services on a commercial basis, as the RFDS believes it needs to make a commercial return on its operations (including properly pricing the risk of its operations). The only real difference between the RFDS and its for-profit competitors is that, instead of profits being returned to shareholders, they are put towards funding the RFDS's other services, which are provided free of charge to the public (or at a subsidised rate).

In relation to other regulatory and external government arrangements placed on NFPs, the RFDS (as with many NFPs providing government funded services) has a number of regulatory and other requirements which are designed to ensure transparency and accountability in its activities in competing with for profit

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organisations for government funded services (and therefore promoting competitive neutrality). These include:

- (iv) government oversight - the RFDS underwent a government review of its cost structures preceding the latest round of Commonwealth funding, to ensure that there is a detailed understanding of what the Commonwealth is funding and how it dovetails into the State and Territory funding;
- (v) government funding arrangements - the RFDS's funding agreement with the Commonwealth contains requirements designed to ensure that Commonwealth funding is not used outside the Commonwealth-funded services, and State and Territory funding agreements contain similar requirements;
- (vi) contractual obligations - the RFDS has extensive transparency and accountability obligations in our government contracts. These are designed to demonstrate that the RFDS provide a value-for-money service, consistent with Commonwealth, State and Territory governance legislation and spending policies, administration costs are minimised, and the RFDS's services are run as an efficient national operation, with economies of scale, providing a seamless service across the country;
- (vii) corporate and business regulation - many large NFPs are corporations and subject to the Corporations Act and other legislation. In this regard, the RFDS is subject to financial accountability and audit requirements, in addition to more general requirements under occupational health and safety, workplace, environmental and other legislation; and
- (viii) service specific regulation - the RFDS is also required to demonstrate that its is meeting rigorous service standards and quality requirements, equivalent to for-profit operations. This is particularly so in the aviation and health sectors, where the RFDS is subject to extensive regulation of pilots, maintenance arrangements and flying operations on the aviation side, and the same is true for its medical operations. None of the RFDS's aircraft operations are run by volunteers, but by professional pilots, doctors and other staff, and therefore there is no advantage to being a not-for-profit organisation in this regard. Other large NFP organisations, particularly in the health sector, are in a similar heavily-regulated position to the RFDS, for example the private hospitals.

In addition, certain state government funding arrangements require the RFDS to demonstrate that no donation funds are applied to the state government contract. The RFDS understands that this requirement may exist as some form of measure to demonstrate competitive neutrality. However, the RFDS questions if this requirement should apply given that for-profit organisations are **not** required to demonstrate that funds from other business activities have not been applied to the contract. This disadvantages NFPs against comparable for-profit organisations. This disadvantage particularly applies to the RFDS as our main sources of income are government contributions and public donations (being ordinary donations and bequests).

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**(f) If not, what features result in unequal treatment and how could it be addressed**

The availability of the income tax exemption and / or the application of funds generated through donations may be perceived as providing the RFDS as an NFP with some form of competitive advantage. However, a company which had tax losses would be in the same position from an income tax point of view, and a company that applied funds or cost savings from other business activities would be no different to the RFDS in applying donation sourced funds.

The risk is that this perception creates a reaction from government that actually creates a commercial disadvantage to the RFDS in favour of the for profit organisation.

**5.3 Effect of government funding on other services provided by NFPs**

The Commission has provided:

*Comments are invited on the effect of government funding on other services offered by not for profit organisations. Are there significant economies of scale and/or scope in service delivery? How important is the capability of some not for profit organisations to deliver an integrated service to the value they generate?*

As outlined above, the RFDS provides emergency aeromedical evacuation services and healthcare clinics in rural and remote areas, and inter-hospital air ambulance services, across the country. The RFDS's operations are funded in part by government funding and in part by public fundraising. Many of the services provided are not solely funded by one or the other. This is because the services that the RFDS provide are often integrated (that is, government funded and charitable) and the RFDS generates economies of scale in providing its services this way. The value is that it allows the RFDS to provide an enhanced and supported government funded service, more targeted to all the needs of its clients.

**(a) Effect of government funding on other services offered by NFPs**

Many government funded projects are subject to separate reporting and acquittal processes. The systems within the RFDS are designed to allow the separation of these costs to provide the integrity of the financial acquittal.

The undertaking of these other projects / services regularly contribute some recovery of administration overheads, thereby allowing the RFDS to apply more resources to its charitable activities. The RFDS considers that other NFPs will have similar experiences.

**(b) Importance to NFPs to deliver an integrated service to the value the NFP generates**

The RFDS has established substantial resources in the aviation and medical areas providing and aerial based medical support and retrieval service covering the major part of regional and remote Australia.

There are a number of economies of scale that are achieved in both the medical and aviation components of the operations. These economies of scale allow the RFDS to deliver a more efficient service across greater areas of Australia.

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Where individual parts of a service are separated and put out for tender, it is important that in the decision to go to tender that the impact on the efficiency and ability to deliver services across a wider range be taken into consideration.

For example the separation of a particular component in one type of service delivery or geographical location to be subject to tender may have the effect of raising the cost per patient of the service delivery in the remainder. The RFDS is not opposed to use of competitive tendering by government but seeks to ensure that the decision process to put a particular component to tender is made having regard to all of the impacts that may flow from that decision.

#### 5.4 Arrangements which promote efficiencies and effectiveness

The Commission has provided:

*Against this background, the comments are invited on the efficiency and effectiveness of arrangements associated with the provision of government funded services. Specifically, the Commission seeks comments on:*

- *opportunities for improving funding and contractual arrangements to promote better outcomes*
- *the effectiveness of existing accountability and reporting requirements, including options for improvement*
- *how changes in service delivery requirements have affected the effectiveness of not for profit organisations and what changes to those requirements might be warranted to enhance their effectiveness*
- *the effectiveness of arrangements for trialling or piloting new approaches to service delivery*
- *the effectiveness of program and service delivery evaluation arrangements*
- *the extent to which governance and reporting requirements associated with funding and contracted arrangements have replaced 'black letter' regulation.*

*Where possible, participants should support their views with evidence. Comments on the extent to which arrangements are necessary to enhance transparency and accountability would also be appreciated.*

The RFDS believes that a focus on the governance arrangements of NFPs would enhance their effectiveness and efficiency.

Over the last ten years the RFDS has devoted efforts and resources to improvements in governance, starting with the Board of Directors and through efficient and effective management teams who are often drawn from the commercial sector.

However, the RFDS is concerned that some NFPs may not be as aware of the importance of governance issues and applying sound business principles. The

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RFDS suggests that NFPs should be encouraged to adopt strong governance standards. Elsewhere in this submission the RFDS has made a suggestion regarding potential improvements to reporting processes. The RFDS suggests that ensuring good governance could be incorporated into reforms to reporting processes.

**(a) Opportunities for improving funding and contractual arrangements**

The RFDS is concerned that Government's recent preference for shorter term contracts for services put out to tender can result in overall increased costs due to the need to factor in the costs of transitioning between providers and start-up costs of new service providers, in areas where significant infrastructure investment is required, such as aviation and medical services.

We suggest that, when setting the proposed term of a contract for a tender process, government would gain greater value if it had regard to the level of investment required for the contractor, and an appropriate period over which that investment may reasonably be recouped without imposing an undue level of additional cost.

**(b) Effectiveness of current accountability and reporting requirements**

As a general comment, there is very little consistency in the accountability and reporting requirements placed on NFPs. Depending on the size of the NFP, its legal status, and the nature of its activities (including what tax concessions it receives), there are varying levels of accountability and reporting requirements, and in some cases, there is overlap. This is especially the case in respect of concurrent Commonwealth and State legislation which each place obligations on the RFDS, creating uncertainty in respect of compliance.

In addition, there are many reporting and accountability mechanisms contained in government funded service contracts which are in addition to, or overlap with, external regulatory requirements.

(i) Examples

We refer the Commission to the submission of Professor McGregor-Lowndes of the Australian Centre for Philanthropy and Not-for-profit Studies at the Queensland University of Technology, lodged in response to the 2008 Senate Inquiry into disclosure regimes for charities and not for profit organisations.

Professor Lowndes has some excellent statistics and examples of the multitude of different reporting requirements and formats across government.

(ii) Options for improvement

The RFDS suggests that there is considerable scope to achieve greater consistency in reporting requirements for NFPs between government departments and agencies, and that this would lead to greater efficiency and reduce costs in the sector.

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