IT 2632 - Income tax: meaning of 'public authority' in definition of 'exempt public body' in division 16D.

TAXATION RULING NO. IT 2632

INCOME TAX: MEANING OF 'PUBLIC AUTHORITY' IN DEFINITION OF 'EXEMPT PUBLIC BODY' IN DIVISION 16D.

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OTHER RULINGS ON THIS TOPIC:

PREAMBLE Division 16D of Part III of the Income Tax Assessment Act 1936 ("the Act"), treats certain non-leveraged finance leases and similar arrangements as if they were loan arrangements. The Division is designed to deny certain deductions to the owners of property where the property concerned (the subject of a non-leveraged finance lease or similar arrangement) is used by, or its use is controlled by, an "exempt public body" or by a person who uses the property outside Australia to produce income which is not subject to Australian tax.

2. The expression "exempt public body" in Division 16D is defined in subsection 159GE(1) to mean:

a. the Commonwealth, a State or a Territory;

b. a municipal authority or other local governing body, the income of which is wholly exempt from tax; or

c. a public authority -

(i) that is constituted by or under a law of the Commonwealth, a State or a Territory; and

(ii) the income of which is wholly exempt from tax.

3. In relation to paragraph (c) of the definition of "exempt public body" in subsection 159GE(1), the purpose of this Ruling is to clarify :

(a) the meaning of the term "public authority";

(b) what is meant by the expression "constituted by or under a law of the Commonwealth, a State or a Territory";

(c) whether a public hospital comes within the scope of paragraph (c) of the definition; and

(d) whether an entity which is wholly owned by a "public authority" is, as a consequence, a "public authority".

RULING Meaning of "Public Authority"

4. The term "public authority" is not defined in the Act. The High Court of Australia has, however, considered the meaning of the term "public authority" in paragraph 23(d).

5. In The Incorporated Council of Law Reporting for the State of Queensland v. FCT (1924) 34 CLR 580, the Court held that the Council which was registered as an association for the purposes of publishing law reports, was not a "public authority" within paragraph 11(1)(a) of the Income Tax Assessment Act 1915-1918. Isaacs ACJ is reported as saying in the course of argument that, for the Council's income to be exempted as that of a "public authority", the Council would have to have been authorised by statute "to act on behalf of the public or of the State" (34 CLR at 585).

6. In Renmark Hotel Inc. v. FCT (1949) 79 CLR 10, Rich J, at first instance, said that the characteristics of a "public authority" within paragraph 23(d) seemed to be that it should carry on under governmental authority some undertaking of a public nature for benefit of the community or a part of it (79 CLR at 18). The community hotel in that case did not conform, in his Honour's judgment, with the general understanding of the term "public authority".

7. On appeal, Latham CJ expressed the opinion that the hotel had not been given any power or authority by State law to do any acts in relation to the public otherwise unauthorised. His Honour regarded as the necessary attributes of a "public authority" the performance of statutory duties and the exercise of public functions (79 CLR at 23). McTiernan J agreed. His Honour saw it as necessary that an entity which claims to be a "public authority" be given, by statute, the powers or duties to be exercised for public objects. Webb J adopted the test of Isaacs J in the Incorporated Council of Law Reporting Case.

8. The High Court's most recent and detailed consideration of the term "public authority" in paragraph 23(d) is in The Western Australian Turf Club v. F. FCT (1978) 139 CLR 288; 78 ATC 4133; 8 ATR 489. The Club in that case became, by the Racing Restriction Act 1917 (WA), the sole licensing body for horse racing in Western Australia. The Act imposed on the Club a public function, that of licensing horse-races throughout the State. This new function was not revenue producing, the Club making no charge for the grant of licenses.

9. Stephen J (with whose reasons Barwick CJ and Jacobs J agreed) stated that the Club had ever since been involved in the exercise of powers and functions not possessed by the ordinary citizen. Its powers and functions had been conferred by statute and were essentially of a public nature. If those powers and functions had been vested in some State authority created for that purpose and having no other function, his Honour thought that it would be a "public authority" for the purposes of paragraph 23(d).

10. Stephen J considered, however, that to confer a public function and powers exercisable in the public interest on a body which had carried on and will continue to carry on, activities not in themselves characteristic of a public authority (i.e. activities of a conventional members' turf club) might not suffice to regard the body as a "public authority".

11. The general approach of the Courts in the Incorporated Council of Law Reporting Case and the Renmark Hotel Case to the question of status as a public authority was regarded by Stephen J as useful. That approach involved a weighing of all relevant circumstances before deciding in particular cases upon the status of the body in question. The possession of some statutory duties or powers is not, Stephen J thought, enough in itself unless, upon examination of all its characteristics, the body can be seen in general to conform to the common understanding of a public authority. In such an examination Stephen J considered that:

(a) it may be profitable to look for features clearly alien to the concept of what is a public authority and to judge to what degree those features are pervasive and important; and

(b) it will be relevant to bear in mind the present statutory context - paragraph 23(d) being a provision granting exemption from income tax to the revenue of local government bodies and public authorities.

12. As the result of a consideration of the following factors, Stephen J was satisfied that the Club was not a "public authority" in the context of that term in paragraph 23(d):

. the Club continued to concern itself with all the varied activities of a major metropolitan turf club, even though it had a new function of a public nature engrafted on to its previous functions;

. those activities were regarded as positively inconsistent with ordinary notions of a public authority; and

. those activities related to the revenue of the Club, which is the special concern of paragraph 23(d).

13. These cases dealt with the meaning of "public authority" in paragraph 23(d). The general approach taken by the High Court in these cases nevertheless provides useful guidance on the

section 159GE(1) definition of "exempt public body" although the meaning of "public authority" within that definition has clearly not been concluded by these High Court decisions.

14. The necessary steps in deciding in particular cases whether a body answers the description of a "public authority" within the Division 16D definition are to:

(a) Weigh all relevant circumstances, especially the nature of the functions of the body concerned, treating the question of the status of the body as essentially a question of fact and degree to be determined in the light of the particular facts of each case.

(b) Consider whether the body has one primary function or a variety of functions not all of which involve the exercise of powers and functions not possessed by the ordinary citizen and which have been conferred by statute and are essentially of a public nature.

(c) Examine all the characteristics of the body to determine whether it can be seen in general to conform to the common understanding of a public authority. To so conform a body would be expected to have public duties, functions or powers to perform and these would ordinarily be carried out under statutory authority for the benefit of the public. While not essential, a distinguishing characteristic is the possession of exceptional powers conferred by statute beyond those possessed by private individuals. However, the derivation of profits for distribution to shareholders or members would not ordinarily be a characteristic of a "public authority". The examination will involve a consideration of:

(i) the significance of any features of the body clearly alien to, or inconsistent with, the concept of what is a public authority; and

(ii) the relevant statutory context, namely, the overall statutory scheme and policy underlying Division 16D.

Meaning of "Constituted By or Under" a Relevant Law

15. Paragraph (c) of the definition of "exempt public body" in subsection 159GE(1) requires a public authority to be "constituted by or under a law of the Commonwealth, a State or a Territory."

16. The ordinary meaning of the word "constitute", according to the Macquarie Dictionary is "to set up or found (an institution etc)." The expression "is constituted" (emphasis added) in subparagraph (c)(i) of the definition of "exempt public body" indicates that the particular organisation or body concerned and its activities must be looked at year by year, and not merely at the time it was first set up or founded. In addition, the

context of the word "constituted", indicates that the particular organisation or body concerned must be constituted as a public authority.

17. The expression "constituted under" a relevant law makes it clear, as Stephen J pointed out in the W.A. Turf Club Case (139 CLR at 293; 78 ATC at 4135; 8 ATR at 492), that an entity need not, from its origin, have possessed those qualities which make it a public authority. It may acquire the necessary attributes subsequently and, if it does so as a result of legislation, it will thereupon have become a public authority that is constituted under the relevant law. His Honour's views apply even more strongly to the expression "constituted by or under" a relevant law in the definition here.

18. The word "constituted" is not equivalent to the word "incorporated". Rich J in the Renmark Hotel Case thought it conceivable that a body, while remaining unincorporated, might yet be constituted under a State Act so as to satisfy the requirements in paragraph 23(d) of the Act for exemption (79 CLR at 19). Barwick CJ in the WA Turf Club Case took the view that it would only be in a rare case, however, that an unincorporated body becomes a public authority by reason of statutory powers or functions given to it (139 CLR at 290; 78 ATC at 4134; 8 ATR at 490).

19. In its context in paragraph (c) of the definition of "exempt public body", the expression "constituted by or under" a Commonwealth, State or Territory law is therefore concerned with the manner in which a body is presently constituted, and not how it was originally constituted. The expression calls for a consideration year by year of whether the body is either set up, founded or established as a public authority by or under the relevant law or, at the relevant date, has acquired the qualities and attributes of a public authority.

Whether a Public Hospital is a Public Authority

20. This Office has considered whether a public hospital constitutes a public authority that is constituted by or under a State law for the purposes of paragraph (c) of the definition of "exempt public body" in subsection 159GE(1).

21. The public hospital in question was founded at a meeting of voluntary workers who were concerned in the 19th century about a lack of adequate hospital care in a major capital city. The hospital was initially operated by a Board of Trustees. Some 50 years later it was incorporated on the enactment of the relevant State legislation and given perpetual succession and independent corporate existence.

22. Bearing in mind that it is the manner in which a body is presently constituted, and not how it was originally constituted, that is relevant, this Office accepts that the public hospital in question now depends on the relevant State legislation for its constitution. The hospital was therefore regarded as a body that is constituted under a State law for the

purposes of the definition of "exempt public body".

23. An examination of the facts and circumstances in which the public hospital operated, revealed that it performed public duties and functions under authority of the relevant State legislation for the benefit of the public. The hospital receives powers and undertakes certain duties as a "public hospital" under the Act in providing health care services to the ill and disadvantaged persons in the community. The public hospital must have a board of management whose functions are to oversee and manage the hospital and to ensure that its services comply with the requirements of the relevant State legislation and the objects of the hospital. The hospital plays a significant role in providing the State's public health services, subject to limited control and reporting on key government policy issues e.g., patient throughput, waiting lists and neo-natal intensive care unit beds. The hospital, in addition to getting grants, subsidies or other financial assistance, from the State Health Department, attracts substantial public donations and manages considerable income for salaried medical practitioners exercising rights of private practice. By and large, the hospital operates autonomously in purchasing or leasing its equipment.

24. The organisation concerned has one primary function (i.e. carrying on a public hospital) rather than a variety of functions some of which do not conform with the normal understanding of a public authority.

25. Considering all the facts and circumstances of the particular public hospital concerned, this Office takes the view that it is a "public authority" for the purposes of the definition of "exempt public body" in subsection 159GE(1). As it is a "public authority", being one "that is constituted by or under a law of ... a State" and having income which is wholly exempt from tax, this Office concluded that the public hospital is an "exempt public body" as defined.

Wholly Owned Entities of Public Authorities

26. Another question this Office has considered is whether an entity which is wholly owned by a public authority is, as a consequence, a public authority.

27. In determining whether the wholly owned entity is a public authority, undue weight should not be placed on the fact that it is wholly owned by a public authority. The wholly owned entity must be able, in its own right, to be described as a public authority after due consideration of the guidelines set out in paragraph 14 of this Ruling. In some circumstances, it may be that the wholly owned entity derives its public functions or powers from the statutory authority which constituted the original public authority. Whether the wholly owned entity is an "exempt public body" for the purposes of Division 16D will also depend upon it, in its own right, satisfying the definition of "exempt public body" in subsection 159GE(1).

COMMISSIONER OF TAXATION
26 April 1991