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Specific Fiscal Risks

Introduction

This chapter describes the specific fiscal risks of the Crown, including contingent liabilities. The risks are disclosed as either quantifiable or unquantifiable, depending on their characteristics. Only contingent liabilities and other specific fiscal risks involving amounts of \$10 million or more in any one year are separately disclosed. Contingent liabilities below \$10 million are included in the “other quantifiable contingent liabilities” total. Comparatives have been adjusted where appropriate to align with the disclosure of new “material” contingent liabilities. The total amount of contingent liabilities remains unchanged.

Specific Fiscal Risks

Specific fiscal risks (excluding contingent liabilities) are a category of Government decisions or circumstances that may have a material impact on the fiscal position. The risks have not been included in the main forecasts because their fiscal impact cannot be reasonably quantified, the likelihood of realisation is uncertain and/or the timing is uncertain. The risks disclosed may not eventuate into Government policy and the final cost or saving may differ from the amount disclosed if the policy is developed.

To ensure a practicable and consistent disclosure approach, risks have been reported that have an expected cost or saving of over \$10 million in any one forecast year and either:

- reflect Government decisions or legislative commitments with uncertain fiscal consequences or timing, or
- are generally being actively considered by the Minister of Finance and responsible Ministers, or
- are decisions that have been deferred until a later date.

The risks outlined in this chapter would, if they eventuate, be considered for funding from the Government’s forecast new operating and capital spending amounts. If the total of all risks considered exceeds the forecast new operating spending amounts in the forecasts, this would impact on the operating balance.

The forecasts incorporate operating and capital forecast spending amounts to accommodate policy initiatives on which decisions have yet to be made. Some risks outlined in this chapter, if they eventuate, would be covered by these amounts and therefore have no impact on the forecasts. These risks have been disclosed to provide an indication of the pressure the risks place upon the forecast spending amounts.

There are a number of other “pressures” on the fiscal position that have not been included as risks. These “pressures” comprise proposals largely generated within individual departments and not yet considered by the Minister of Finance and responsible Ministers. Such items are also expected to be managed within the forecast spending amounts noted above.

Specific fiscal risks do not include:

- normal forecasting risks, such as uncertainty around welfare benefits, SOE/Crown entity surpluses, the impact of regular revaluations of physical assets, finance costs, or fluctuations in external markets
- possible changes to the interpretation of accounting policies, such as the changes to revenue recognition rules and recognition of liabilities
- discussion documents containing proposals that the Minister of Finance and responsible Ministers will not actively consider until the consultation process has been completed.

The Fiscal Responsibility Act 1994 requires that all specific fiscal risks be disclosed, except where it is determined by the Minister of Finance that disclosing a risk is likely to:

- prejudice the substantial economic interests of New Zealand, or
- prejudice the security or defence of New Zealand or international relations of the Government, or
- compromise the Crown in a material way in negotiation, litigation or commercial activity, or
- result in a material loss of value to the Crown.

In addition, the Minister of Finance has to determine that there is no reasonable or prudent way the Government can avoid this prejudice, compromise or material loss by making a decision on the fiscal risk before the finalisation of the forecasts, or by disclosing the fiscal risk without reference to its fiscal implications.

Time-Limited Funding

Time-limited funding does not meet the definition of a “risk” under the Fiscal Responsibility Act, but is further information that is prepared to increase transparency about initiatives with funding profiles that cease or decrease during the forecast period.

The following table outlines those areas where initiatives have time-limited funding that decreases or ceases at some point, using a \$5 million materiality threshold. They are often related to pilot programmes that may or may not be extended. If operating funding were to be appropriated to maintain funding levels for these five initiatives (ie, extend the initiative beyond its current scheduled completion date), the total impact would be up to \$20 million in 2003/04, \$40 million in 2004/05 and \$46 million from 2005/06, which would impact on the operating balance.

Vote	Description of initiative	Operating impact (\$million)
Education	Microsoft Software Licensing	2 in 2003/04, 5 from 2004/05
Education	Tertiary Education Commission	9 from 2004/05
Education	Tertiary Education Strategic Change Fund	18 from 2003/04
Internal Affairs	Weathertight Homes Resolution Service	5 in 2004/05, 8 from 2005/06
Māori Affairs	Direct Resourcing of Local-Level Solutions	3 in 2004/05, 6 from 2005/06

Statement of Specific Fiscal Risks

The fiscal risks included in the following tables were finalised as at 1 May 2003.

Quantified Risks¹

The risks outlined in these tables would, if they eventuate, be considered for funding from the Government's forecast new operating and capital spending amounts.

Risks as at 1 May 2003	Operating balance	Gross debt	Net worth	(\$ million)
New risks				
Customs – Container security	Decrease	Increase	Decrease	-20 operating from 2004/05
Government response to Growth and Innovation Framework Sector Taskforces	Decrease	Increase	Decrease	-110 operating over 4 years
Revenue – Tax simplification for Small and medium enterprises	Decrease	Increase	Decrease	-20 operating from 2004/05
Tourism – Marketing opportunities with Team New Zealand	Decrease	Increase	Decrease	-34 operating over 4 years
Changed Risks				
ACC – Medical Misadventure review	Decrease	Increase	Decrease	-25 operating from 2003/04
Corrections – Capital projects	Decrease	Increase	Decrease	-398 capital over 4 years -110 operating over 4 years
Education – ECE Strategic Plan	Decrease	Increase	Decrease	-120 operating over 4 years
Education – School property	Decrease	Increase	Decrease	-75 capital in 2003/04; -115 in 2004/05 and outyears -1 operating in 2003/04; -8 in 2004/05; -21 in 2005/06; and -30 in 2006/07
Education – United Nations Convention on the Rights of the Child	Decrease	Increase	Decrease	-14 operating from 2003/04
Health – District health board deficits	Decrease	Increase	Decrease	-120 operating in 2003/04 and -46 in 2004/05
Unchanged risks				
Agriculture and Forestry – painted apple moth	Decrease	Increase	Decrease	-24 operating in 2003/04; -16 in 2004/05; -3 in 2005/06; and -1 in 2006/07
Defence – Capital injections	Decrease	Increase	Decrease	-713 capital over 4 to 9 years
Health – Mental Health Blueprint	Decrease	Increase	Decrease	-25 operating in 2004/05; -50 in 2005/06; and -75 in 2006/07
Revenue – Risk Free Return Method	Increase	Decrease	Increase	20 operating from 2004/05

1 In the summary tables listing specific risks:

- negative numbers indicate a deterioration in the Crown's financial position
- "N/A" means no effect
- "Unclear" means insufficient information is available to determine the risk's effect.

In this chapter, "Gross Debt" refers to gross sovereign-issued debt.

Unquantified Risks

The risks outlined in this table would, if they eventuate, be considered for funding from the Government's forecast new operating and capital spending amounts.

Risks as at 1 May 2003	Operating balance	Gross debt	Net worth
<i>New risks</i>			
Child, Youth and Family – Baseline review	Decrease	Increase	Decrease
Education – Collective employment agreements	Decrease	Increase	Decrease
Gas Supply	Decrease	Increase	Decrease
Foreign Affairs and Trade – Ministry of Foreign Affairs and Trade capability	Decrease	Increase	Decrease
Foreign Affairs and Trade – Official Development Assistance	Decrease	Increase	Decrease
Health – Payments for family members as caregivers	Decrease	Increase	Decrease
Health – Wage bargaining	Decrease	Increase	Decrease
Housing – Housing Strategy	Decrease	Increase	Decrease
Immigration – Immigration Policy	Unclear	Unclear	Unclear
Police – Wage bargaining	Decrease	Increase	Decrease
Revenue – Fringe benefit tax review	Unclear	Unclear	Unclear
Revenue – Taxation of foreign direct investment	Decrease	Increase	Decrease
<i>Changed risks</i>			
Air New Zealand	Unclear	Unclear	Unclear
Corrections – Output price review	Decrease	Increase	Decrease
Education – Wananga capital injection	N/A	Increase	N/A
Revenue – Taxation of savings and investment vehicles, including superannuation funds	Unclear	Unclear	Unclear
Social Development – Benefit payment systems	Decrease	Increase	Decrease
Social Development – Response to Joychild Report	Decrease	Increase	Decrease
<i>Unchanged risks</i>			
Climate Change and Energy Efficiency – Climate change	Unclear	Unclear	Unclear
Conservation – Recognition of fencing on the Conservation Estate	Decrease	Increase	Decrease
Defence – Sale of Skyhawks and Aermacchi trainers	Increase	Decrease	Increase
Education – Capital injections for tertiary education institutions	Decrease	Increase	Decrease
Education – Improved Internet access – Project Probe	Decrease	Increase	Decrease

Unquantified Risks (continued)

Education – Partnerships for Excellence	Decrease	Increase	Decrease
Housing – State housing project at Hobsonville	Decrease	Increase	Decrease
Police – Capital projects	Decrease	Increase	Decrease
Revenue – Exemption for overseas earnings	Unclear	Unclear	Unclear
Revenue – Gaming Review	Unclear	Unclear	Unclear

Risks Removed Since the 2002 December Update

Risks	Comment
Agriculture and Forestry – Sustainable Farming Fund	In baselines
Courts – Supreme Court	In baselines
Education – Tertiary education funding	Not under active consideration
Energy Efficiency and Conservation – National Energy Efficiency and Conservation Strategy	In baselines
Environment – Climate change institutional arrangements	In baselines
Health – Forecast financial track	In baselines
Health – Remove asset testing from long-stay care	In baselines
Internal Affairs – Weathertight Homes Resolution Service	In baselines
Revenue – GST and imported services and financial services review	In baselines
Revenue – Trans-Tasman triangular tax relief	In baselines
Transport – Lease of rail assets	In baselines

Quantified Fiscal Risks

New risks

Customs – Container security (new risk)

The Government has approved operating and capital funding in 2003/04 to provide real-time risk assurance and, where necessary, X-ray screening of export containers. The Government has yet to determine the appropriate arrangements for meeting operating costs in 2004/05 and outyears. The ongoing operating cost is expected to be up to \$20 million in 2004/05 and outyears, which would decrease the operating balance.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

The Minister of Finance has yet to fully consider the quantum of this risk.

Source: New Zealand Customs Service

Government response to Growth and Innovation Framework Sector Taskforces (new risk)

The Government has established four Sector Taskforces to look into issues affecting growth in the following sectors: Information and Communications Technology; Biotechnology; Screen Production; and Design. The Taskforces are at various stages of finalising their reports and are expected to make recommendations to the Government by the end of May 2003.

The Government will not be in a position to consider these recommendations until mid-2003, but the estimated cost of responding to the recommendations is around \$110 million over four years, which would decrease the operating balance. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Revenue – Tax simplification for small and medium enterprises (new risk)

The Government intends releasing a discussion document in mid- to late 2003 containing proposals to reduce tax compliance costs for small to medium enterprises. Depending upon the composition of the package of measures decided after consultation on the discussion document, the proposals may have a fiscal cost of between \$20 million and \$40 million per year, commencing at the earliest from 2004/05.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

The Minister of Finance has yet to fully consider the quantum of this risk.

Source: Inland Revenue

Tourism – Marketing opportunities with Team New Zealand (new risk)

The Government announced that it has initially committed \$5.625 million to Team New Zealand to retain team members for the 2007 America's Cup in Europe.

The Government will commit up to a maximum of \$34 million in total as a marketing partner for the challenge. The final level of the Government's contribution will depend on an assessment of the potential economic benefits that can be leveraged off the next regatta in Europe and Team New Zealand's ability to raise substantial funding from the private sector.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Changed risks

ACC – Medical Misadventure review (changed risk)

The Medical Misadventure Account is currently funded partly from the Earners' Account and partly by the Crown through the Non-Earners' Account. A review of the Medical Misadventure Account is underway, considering all aspects of the Account. Potential costs resulting from the Review range from zero to \$47 million, some of which will be covered by ACC Earners' Levy payers.

The potential impact on the operating balance ranges from zero to a decrease of \$25 million per annum from 2003/04 (unquantified in the *December Update*). This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

The Minister of Finance has yet to fully consider the quantum of this risk.

Source: Accident Compensation Corporation

Corrections – Capital projects (changed risk)

The Department of Corrections has estimated that a total of \$398 million of capital injections and operating funding of \$110 million (\$422 million and \$79 million respectively in the *December Update*) will be required over the forecasting period for capital projects to meet future prison muster forecasts.

The actual amounts will depend on the specification and timing of the individual projects and the contracted prices. These estimates include consideration of funding for the:

- Spring Hill Corrections Facility
- Otago Men's Corrections Facility
- Mt Eden Prison
- Auckland Women's Corrections Facility.

Capital injections would increase gross debt while operating funding would decrease the operating balance. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

The Minister of Finance has yet to fully consider the quantum of these risks.

Source: Department of Corrections

Education – ECE Strategic Plan (changed risk)

The Early Childhood Education (ECE) Strategic Plan, which sets out a 10-year action plan for the sector, was released in September 2002. This Plan signals major changes to the funding, regulation and ownership of ECE services. The Government is considering a number of issues related to implementation details, flow-on effects of kindergarten teachers' pay parity, and the balance of Government funding/parent fees.

These decisions may require operating funding that is estimated up to \$120 million by 2006/07 (\$50 million in the *December Update*) and would decrease the operating balance. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

The Minister of Finance has yet to fully consider the quantum of this risk.

Source: Ministry of Education

Education – School property (changed risk)

The Government has provided \$38 million in 2003/04 for school accommodation in the 2003 Budget. Additional capital injections for school accommodation are likely to be required in future years to meet roll growth. Capital injections are estimated to be up to \$75 million in 2003/04 and \$115 million in 2004/05 and each subsequent outyear (\$194 million and \$185 million respectively in the *December Update*).

In addition to capital injections, consequential operating costs are likely to be incurred. These are estimated at \$1 million in 2003/04, \$8 million in 2004/05, \$21 million in 2005/06 and \$30 million in 2006/07 (\$8 million, \$31 million, \$40 million and \$44 million respectively in the *December Update*).

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

The Minister of Finance has yet to fully consider the quantum of this risk.

Source: Ministry of Education

Education – United Nations Convention on the Rights of the Child (changed risk)

The United Nations Convention on the Rights of the Child obliges New Zealand to confer the rights of the Convention on all children. New Zealand has reserved its right to distinguish between persons according to the nature of their authority to be in New Zealand. However, the Government has indicated that it will undertake work to see if this reservation can be removed. This would involve making some changes to eligibility for some health and education services, which may decrease the operating balance by approximately \$14 million per year (\$9 million in 2003/04 and \$14 million in 2004/05 and outyears in the *December Update*).

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

The Minister of Finance has yet to fully consider the quantum of this risk.

Source: Ministry of Education

Health – District health board deficits (changed risk)

The Government announced a transition path to Population Based Funding for district health boards (DHBs) on 21 November 2002. This changed funding path will result in substantially reduced DHB forecast deficits. Initial draft District Annual Plans for 2003/04 to 2005/06 indicate deficits of approximately \$120 million in 2003/04 and \$46 million in 2004/05 (\$90 million and \$110 million respectively in the *December Update*). The Government has not accepted the size of these forecast deficits and is actively discussing actions and cost-containment measures with these DHBs to manage back the deficits at the same time as maintaining service levels.

The impact on the operating balance, if any, is unclear. Any deficits above that provided for within the health funding allocation will decrease the operating balance and increase gross debt. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

The Minister of Finance has yet to fully consider the quantum of this risk.

Source: Ministry of Health

Unchanged risks*Agriculture and Forestry – Painted apple moth (unchanged risk)*

The Government has approved funding for 2002/03 to pursue eradication of painted apple moth by aerial spraying up to 12,000 hectares. The Ministry of Agriculture and Forestry has developed programme milestones to enable it to monitor progress towards eradication including scope and likelihood of success. It will report back in May 2003 on the outcome of this programme with a recommendation on whether to continue with the programme. If the Government decides to continue to pursue eradication then additional outyear funding will be necessary.

The operating funding required is estimated at \$24 million in 2003/04, \$16 million in 2004/05, \$3 million in 2005/06 and \$1 million in 2006/07, which would decrease the operating balance. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

The Minister of Finance has yet to fully consider the quantum of this risk.

Source: Ministry of Agriculture and Forestry

Defence – Capital injections (unchanged risk)

Implementing the Government's decisions on the future force structure of the New Zealand Defence Force (NZDF) will involve a series of capital acquisitions across all three armed services to achieve the required capability upgrades. The Government has agreed to a capital injection of up to \$1 billion over 2001/02 to 2010/11, of which \$287 million has been agreed, with the bulk likely to be required within the next four years to enable these acquisitions to occur. The actual expenditure profile will depend on the specification and timing of the individual projects, the contracted prices, and the prevailing exchange rate at the time of purchase.

The Minister of Finance is engaged in a process to consider the individual projects of this risk as they occur. Any capital injections would increase gross debt. This risk would, if it

eventuates, be considered for funding from the Government's forecast new capital spending amount.

Source: New Zealand Defence Force

Health – Mental Health Blueprint (unchanged risk)

The Mental Health Blueprint recommends an increasing funding profile for mental health services. This growth in funding has been included in forecasts to 2003/04, which was the furthest it could be extended to at the time the decision was taken. The Government is expected to consider further increases outside the Health Funding Path of \$25 million in 2004/05, \$50 million in 2005/06 and \$75 million in 2006/07, which would decrease the operating balance.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Source: Ministry of Health

Revenue – Risk Free Return Method (unchanged risk)

The Government is considering the application of the Risk Free Return Method of taxation to equity investments on capital account or outside a business context. A number of details of the proposal need to be further developed and, if a decision to proceed is taken, the proposal will be subject to full consultation, so it is not expected to be implemented before the 2004/05 tax year.

Although the impact on the operating balance is unclear at this stage, it is expected that this would increase the operating balance by between \$20 million and \$40 million per year. This risk would, if it eventuates, be considered against the Government's forecast new operating spending amount.

The Minister of Finance has yet to fully consider the quantum of this risk.

Source: Inland Revenue

Unquantified Fiscal Risks

New risks

Child, Youth and Family – Baseline review (new risk)

In December 2002 the Government directed officials to carry out a first-principles baseline review of Vote Child, Youth and Family Services and report back by the end of August 2003.

The risk is unquantified as the amount or timing of any change in departmental funding is unclear, but any increase in funding to meet additional operating costs would decrease the operating balance and any new capital contributions would increase gross debt.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

Education – Collective employment agreements (new risk)

The primary, secondary and area school principals' collective agreements expired on 30 April 2003. The Crown will need to meet any fiscal impact in 2003/04 and beyond due to the renegotiation of these agreements. Any increase in funding required will decrease the operating balance.

This risk is unquantified, as disclosure could compromise the Crown in negotiations. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Gas Supply (new risk)

The Government is considering options to improve certainty of gas supply, including for electricity generation. This involves direct negotiations with industry parties.

This risk is unquantified as disclosure could compromise the Crown in negotiations and commercial activities. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Foreign Affairs and Trade – Ministry of Foreign Affairs and Trade capability (new risk)

The Ministry of Foreign Affairs and Trade identified funding pressures during the 2003 Budget process. The Government has deferred a decision on whether additional resources are required until after a review of the Ministry's capability needs is completed in June 2003.

The risk is unquantified as the amount or timing of any change in departmental funding is unclear, but any increase in funding to meet additional operating costs would decrease the operating balance and any new capital contributions would increase gross debt.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

Foreign Affairs and Trade – Official Development Assistance (new risk)

The Government is considering increasing the aid budget as and when resources allow, in line with United Nations commitments. This will involve looking at a range of options for increasing and allocating any additional funding, which would decrease the operating balance.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Health – Payments for family members as caregivers (new risk)

The Human Rights Review Tribunal has determined that the practice of not paying family members providing custodial care to their own family was not based on written policy. Several government agencies (Ministry of Social Development, Ministry of Health, ACC, Child, Youth and Family Service) are now involved in developing Terms of Reference for a review to consider possible policy responses to this decision. The risk is unquantified as policy options have yet to be developed and the amount and timing of any change in funding have yet to be determined. Any increase in funding to providers would decrease the operating balance.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Health – Wage bargaining (new risk)

The New Zealand Nurses' Organisation has indicated it will be seeking substantial pay increases in upcoming wage negotiations. The Minister of Health has indicated to DHBs that the outcome of these negotiations must be met within their three-year Health Funding Paths. If this were not the case it would decrease the operating balance or increase gross debt (via DHB deficits).

This risk is unquantified, as disclosure could compromise the Crown in negotiations. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

Housing – Housing Strategy (new risk)

In December 2002 the Government agreed that HNZC would develop a Housing Strategy involving consultation with all key stakeholders in the housing and wider social sectors.

The risk is unquantified as the amount or timing of any change in departmental funding is unclear, but any increase in funding to meet additional operating costs would decrease the operating balance and any new capital contributions would increase gross debt.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

Immigration - Immigration Policy (new risk)

The Government has made some high-level decisions about business immigration policies and is presently considering a number of implementation issues. The impacts on the operating balance and debt are unclear as they depend on the options chosen.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Police – Wage bargaining (new risk)

The current Police pay award expires on 30 June 2003. The outcome of negotiations for the 2003 wage round and impact on baselines are unknown at this stage but are likely to reduce the operating balance.

This risk is unquantified, as disclosure could compromise the Crown in negotiations. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Revenue – Fringe benefit tax review (new risk)

The Government has decided to review the fringe benefit tax regime. The review will focus on reducing the difficulty and cost to employers of complying with fringe benefit tax, while ensuring the revenue base is maintained. Any legislative changes resulting from the review will be introduced in 2004.

Any impact on the operating balance from any legislative amendments is unclear at this stage. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Revenue – taxation of foreign direct investment (new risk)

The Government is considering its response to the recommendations regarding the taxation of foreign direct investment of the Tax Review 2001, including its recommendation that headline company tax rates for foreign investors be reduced to 18%.

Details of any response need to be further developed and would not be expected to apply before 2004/05. However, the overall impact of any measures if adopted would be to reduce the operating balance. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Changed risks*Air New Zealand (changed risk)*

Air New Zealand and Qantas have announced they wish to form a strategic alliance, with Qantas acquiring a minority equity interest in Air New Zealand. Competition authorities (the Commerce Commission in New Zealand and the Australian Competition and Consumer Commission) are currently considering the proposal. The draft determinations issued by these bodies in April 2003 indicated that on the basis of information currently available, the authorities could not be satisfied that the public benefits from the proposed alliance would outweigh the detriment. Further analysis and consideration will now be undertaken before final determinations are issued.

Should the proposal proceed, there may be an impact on the Government's share of Air New Zealand's future earnings, which would impact on the operating balance. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Corrections – Output price review (changed risk)

The Ministers of Finance and Corrections have agreed to undertake an output price review to determine the appropriate output prices required to sustain the medium-to-long term ability of the Department of Corrections to deliver the quality and quantity of outputs required by the Government.

Funding of \$15 million per annum was agreed in the 2003 Budget to fund immediate cost and volume pressures and to enhance the capability of the Community Probation Service. Residual funding pressures will be addressed in the 2004 Budget.

The risk is unquantified as the amount or timing of any change in departmental funding is unclear, but any increase in funding to meet additional operating costs would decrease the operating balance and any new capital contributions would increase gross debt.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

Education – Wananga capital injection (changed risk)

Ministers are currently negotiating with one wananga (Māori tertiary institution) (two wananga in *December Update*) over settlement of its Waitangi Tribunal claim. The Waitangi Tribunal has recommended that the wananga be compensated for capital expenditure that has been incurred on facilities to date, and be provided with funding to bring its facilities up to a standard comparable with other tertiary institutions and to meet additional capital requirements. Any capital injection will increase gross debt.

The fiscal risk is unquantified as disclosure could compromise the Crown in negotiations. This risk would, if it eventuates, be considered for funding from the Government's forecast new capital spending amount.

Revenue – Taxation of savings and investment vehicles, including superannuation funds (changed risk)

The Government has agreed to measures to improve the tax environment for savings through changes to employer contribution schemes by matching the withholding tax paid by employers to the statutory marginal rate paid by workers below \$38,000 in income. It is now considering the broader issue of whether the tax system creates impediments to adequate saving and whether current taxation of retirement saving is equitable.

The impact of any proposal on the operating balance would vary widely by the options chosen and the method of implementation. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Social Development – Benefit payment systems (changed risk)

The Ministry of Social Development is considering the future development and/or replacement of its income benefit payment systems (SWIFTT and TRACE). Decisions will

be made when an IT strategy has been developed taking into account the Ministry's Statement of Intent and the results of the work on the reform of the social assistance system. This planning sequence is the reason for the change from the risk reported in the *December Update* (cost of \$33 million to \$91 million assumed in 2003/04).

Capital injections for development costs will have an impact on debt, and operating funding will affect the operating balance. The quantum of the risk cannot be determined until decisions have been made about which options are to be chosen. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

Social Development – Response to Joychild Report (changed risk)

The Government is reviewing cases where a debt was established against a Domestic Purposes Benefit recipient between November 1996 and December 2000, to ensure that appropriate legal tests were used in establishing the debts. The opportunity to lodge an appeal closed on 31 March 2003 and by then 5,657 people had asked that their cases be reviewed.

The potential costs of reviewing the cases, and of rectifying any cases where the review finds that a debt was improperly established, cannot be determined until the review process starts. Any operating funding required would decrease the operating balance.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Unchanged risks

Climate Change and Energy Efficiency – Climate change (unchanged risk)

The Government has ratified the Kyoto Protocol, and has approved a policy package to meet commitments under the Protocol. The package contains the following elements, which will be targeted at different sectors as appropriate and may be funded through cash or emission units:

- Existing policies aimed at greenhouse gas reduction, including the waste strategy, renewables programme, and the energy efficiency and conservation strategy.
- A carbon charge with negotiated greenhouse agreements for those firms deemed to be "competitiveness at risk".
- Emissions' reduction projects.
- Methane and nitrous oxide mitigation research.
- Mechanisms to incentivise establishment and enhancement of carbon sinks.

At this stage, it is unclear what impact the decision to ratify the Protocol will have on the operating balance, either positive or negative, since this is closely related to the detailed design of the policy options.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Conservation – Recognition of fencing on the Conservation Estate (unchanged risk)

The Department of Conservation is undertaking a project to identify all fences on the Conservation Estate. This requires each fence to be inspected and valued and ownership clarified as some fences will be on land with adjoining owners. The recognition of these assets will increase the Crown's net worth.

At this stage, it is not known what the value will be. Future operating costs will be considered at the end of the project. Any additional operating funding will reduce the operating balance and capital injections would increase gross debt.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating and capital spending amounts.

Defence – Sale of Skyhawks and Aermacchi trainers (unchanged risk)

As a result of the Government's decisions on the future force structure of the NZDF, the NZDF is in the process of selling the Skyhawks and Aermacchi trainers. These sale proceeds would increase the operating balance and decrease gross debt.

This risk is unquantified as disclosure could compromise the Crown in the sale process. This risk would, if it eventuates, be considered against the Government's forecast new operating and capital spending amounts.

Education – Capital injections for tertiary education institutions (unchanged risk)

Several tertiary education institutions are facing financial pressure. They may seek assistance from the Government as they develop their plans for the future. The risk is unquantified as the amount or timing of any request for financial assistance is unclear.

This risk would, if it eventuates, be considered for funding from the Government's forecast new capital spending amount.

Education – Improved Internet access – Project Probe (unchanged risk)

The Government is considering options to improve high-speed Internet access to all schools and their communities. This risk is unquantified as negotiations with providers are still progressing. The costs associated with this proposal would decrease the operating balance.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Education – Partnerships for Excellence (unchanged risk)

The Government has decided to establish an arrangement called "Partnerships for Excellence" whereby the Crown matches private sector investment in the tertiary sector. This risk is unquantified as funds will be considered on an annual basis subject to budgetary pressures. Any capital injections will increase gross debt.

This risk would, if it eventuates, be considered for funding from the Government's forecast new capital spending amount.

Housing – State housing project at Hobsonville (unchanged risk)

The Government has announced that HNZC will acquire, under the Housing Act 1955, NZDF land at Hobsonville deemed surplus to defence requirements but suitable for state housing purposes. The land is expected to become available over the next three to four years.

Depending on development options taken and timing, the Corporation may require additional capital from the Crown, which would increase gross debt. This risk would, if it eventuates, be considered for funding from the Government's forecast new capital spending amount.

Police – Capital projects (unchanged risk)

New Zealand Police has identified a number of Police stations that require capital work to bring them up to a modern operating standard.

The timing, scale and funding for new assets are unclear at this stage, but any capital injections would increase gross debt. This risk would, if it eventuates, be considered for funding from the Government's forecast new capital spending amount.

Revenue – Exemption for overseas earnings (unchanged risk)

The Government is considering options to encourage skilled migrants to come to New Zealand, including the introduction of a time-limited exemption for overseas earnings for new migrants. Details of the proposal need to be further developed and the proposal will be subject to consultation, so it is not expected to be implemented before 2004/05.

The impact, if any, of this proposal on the operating balance is unclear as it depends on the options chosen. This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Revenue – Gaming Review (unchanged risk)

The Gaming Review was completed and the Responsible Gambling Bill is before Parliament. The Government has yet to consider the taxation of gaming. Any impact on the operating balance arising from a response, whether positive or negative, is unclear.

This risk would, if it eventuates, be considered for funding from the Government's forecast new operating spending amount.

Contingent Liabilities

Contingent liabilities are costs that the Crown will have to face if a particular event occurs. Typically, contingent liabilities consist of guarantees and indemnities, legal disputes and claims, and uncalled capital. The contingent liabilities facing the Crown are a mixture of operating and balance sheet risks, and they can vary greatly in magnitude and likelihood of realisation. In general, if a contingent liability were realised it would reduce the operating balance and net worth, and increase net Crown debt. However, in the case of contingencies for uncalled capital, the negative impact would be restricted to net Crown debt.

Where contingent liabilities have arisen as a consequence of legal action being taken against the Crown, the amount shown is the amount claimed and thus the maximum potential cost. It does not represent either an admission that the claim is valid or an estimation of the possible amount of any award against the Crown.

Contingent liabilities have been stated as at 31 March 2003, being the last set of published contingent liabilities.

Details of each of the following contingent liabilities can be accessed from the Treasury website at <http://www.treasury.govt.nz/forecasts/befu2003>.

Quantifiable Contingent Liabilities

Guarantees and indemnities	Status²	(\$ million)
Cook Islands – Asian Development Bank loans	Changed	20
Indemnification of receivers and managers – Terralink Limited	Unchanged	10
Indemnification of touring exhibitions	Changed	140
Ministry of Transport – funding guarantee	Unchanged	10
Post Office Bank – guaranteed deposits	Unchanged	14
Guarantees and indemnities of state-owned enterprises and Crown entities	Unchanged	23
Other guarantees and indemnities	Changed	43
		260
Uncalled capital		
Asian Development Bank	Changed	1,215
European Bank for Reconstruction and Development	Unchanged	14
International Bank for Reconstruction and Development	Changed	1,484
		2,713
Legal proceedings and disputes		
Health – legal claims	Changed	119
Police – legal claims	Changed	32
Tax in dispute	Changed	40
Legal proceedings and disputes of state-owned enterprises and Crown entities	Unchanged	34
Other legal claims	Changed	65
		290
Other quantifiable contingent liabilities		
International finance organisations	Changed	1,318
Reserve Bank – demonetised currency	Unchanged	23
Other quantifiable contingent liabilities of state-owned enterprises and Crown entities	Changed	144
Other quantifiable contingent liabilities	Changed	41
		1,526
Total quantifiable contingent liabilities		4,789

2 Relative to reporting in the 31 December 2002 Crown financial statements.

Unquantifiable Contingent Liabilities

Institutional guarantees	Status
Air New Zealand Limited	Unchanged
Asure New Zealand Limited	Unchanged
At Work Insurance Limited	Unchanged
Auckland rail lease	Unchanged
Commerce Commission – indemnity for damages	Unchanged
Crown research institutes	Unchanged
DFC New Zealand Limited (under statutory management)	Unchanged
District Court Judges, Justices of the Peace, Coroners and Disputes Tribunal	Unchanged
District health boards	Unchanged
Earthquake Commission	Unchanged
Electricity Corporation of New Zealand Limited	Unchanged
Fletcher Challenge Limited	Unchanged
Housing New Zealand Corporation	Unchanged
Indemnities against acts of war and terrorism	Unchanged
Maui Partners	Unchanged
Ministry of Agriculture and Forestry – indemnity provided for the eradication of the painted apple moth	New
Ministry of Fisheries – indemnity provided for delivery of registry services	Unchanged
National Provident Fund	Changed
New Zealand Railways Corporation	Unchanged
Persons exercising investigating powers	Unchanged
Pharmaceutical Management Agency Limited – indemnity	Unchanged
Public Trust	Unchanged
Purchasers of Crown operations	Unchanged
Reserve Bank of New Zealand	Unchanged
Tainui lease guarantees	New
Tax liabilities	Unchanged
Works Civil Construction	Unchanged
Works Consultancy Services	Unchanged

Unquantifiable Contingent Liabilities (continued)

Other unquantifiable contingent liabilities	
Accident Compensation Corporation	Unchanged
Education – legal claim	Unchanged
Education – fees collected on behalf of members of the Māori University Students Association	Unchanged
Environmental liabilities	Unchanged
New Zealand Post Primary Teachers' Association	Unchanged
Sale of Crown assets	Unchanged
Treaty of Waitangi claims	Unchanged
Treaty of Waitangi claims – settlement relativity payments	Unchanged