

# 4

---

## Specific Fiscal Risks

### Introduction

This chapter describes the specific fiscal risks to the Crown, including contingent liabilities. PFA requires disclosure of all government decisions and other circumstances that may have a material effect on the fiscal and economic outlook.

### Criteria for Disclosure of Specific Fiscal Risks

To ensure a practicable and consistent disclosure approach, fiscal risks are disclosed based on the following criteria, consistent with the principles of the PFA:

- *Reasonable certainty criterion* – risks have not been included in the fiscal forecasts because they reflect Government decisions or legislative commitments with uncertain fiscal consequences or timing.
- *Materiality criterion* – risks have an impact on the fiscal forecasts (operating balance, net worth or gross debt) of \$10 million or more in any one forecast year.
- *Active consideration criterion* – risks are being actively considered by the Minister of Finance and responsible Ministers (ie, are the subject of written reports) or are decisions that have been deferred until a later date.

### Exclusions from Disclosure

The PFA 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.

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.

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.

Contingent liabilities are also included according to materiality. 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.

## Information Relating to All Disclosed Risks

- 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.
- All risks, should they eventuate, would impact on the Government’s forecast operating and/or capital spending amounts. These are forecast spending amounts already incorporated into the forecasts to accommodate policy initiatives on which decisions have yet to be made. Most risks outlined in this chapter, if they eventuate, would be covered by these amounts and therefore have no impact on the forecasts. The risks have been disclosed to indicate the pressure the risks place upon the forecast 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.
- 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 expected to be managed within forecast spending amounts noted above.
- All quantified risks are stated GST exclusive, in accordance with the amendments to the PFA. This differs from the *December Update*, where risks were GST inclusive.

## Charges against Future Budgets

As part of its Budget strategy, the Government has put in place some longer-term funding paths for particular sectors. This aids long-term planning and demonstrates the Government’s commitment to specific policies.

Charges against future Budgets do not meet the definition of a “risk” under the PFA, as these items are incorporated in the fiscal forecasts. This section is provided to increase transparency about the provisions for future Budgets.

### *Defence Sustainability Initiative*

The Defence Sustainability Initiative (DSI) is designed to provide the New Zealand Defence Force (NZDF) with the funding required to address issues identified by the Defence Capability and Resourcing Review, including capability, and maintaining equipment and reserves. Budget 2005 includes \$60 million per annum as the first tranche of the 10-year plan. The following table shows the additional tranches as charged against future Budgets.

<b>Budget to be Charged (\$m)</b>	<b>06/07</b>	<b>07/08</b>	<b>08/09</b>	<b>09/10</b>	<b>10/11</b>	<b>11/12</b>	<b>12/13</b>	<b>13/14</b>	<b>14/15</b>
Budget 2006	79.5	72.8	72.8	72.8	72.8	72.8	72.8	72.8	72.8
Budget 2007		58.0	58.0	58.0	58.0	58.0	58.0	58.0	58.0
Budget 2008			69.1	69.1	69.1	69.1	69.1	69.1	69.1
Budget 2009				85.7	85.7	85.7	85.7	85.7	85.7
Budget 2010					108.1	108.1	108.1	108.1	108.1
Budget 2011						66.9	66.9	66.9	66.9
Budget 2012							14.2	14.2	14.2
Budget 2013								58.6	54.2
Budget 2014									0

### *Health Funding Package*

In Budget 2005, the health sector has received \$475 million per annum as the third tranche of the Health Funding Package (HFP). A fourth tranche of \$489 million per annum is charged against Budget 2006.

<b>Budget to be Charged (\$million)</b>	<b>2006/07</b>	<b>2007/08</b>	<b>2008/09</b>	<b>2009/10 and Outyears</b>
Budget 2006	489	489	489	489

### **Official Development Assistance**

The Government has committed to an Official Development Assistance to Gross National Income ratio (ODA:GNI ratio) of 0.27% for the fiscal years 2005/06 and 2006/07 and increasing this to 0.28% in 2007/08. Budget 2005 includes funding for 2005/06 levels only. The 0.27% in 2006/07 is expected to cost an additional \$19 million per annum to be charged against Budget 2006, and the 0.28% in 2007/08 is expected to cost \$38 million to be charged against Budget 2007.

<b>Budget to be Charged (\$million)</b>	<b>2006/07</b>	<b>2007/08</b>	<b>2008/09</b>	<b>2009/10 and Outyears</b>
Budget 2006	19	19	19	19
Budget 2007		38	38	38

### **Tertiary Student Component Funding Rate Changes (The rolling funding triennium and fee and course cost maxima)**

The Government has a policy of increasing Student Component funding rates for tertiary education by the rate of forecast CPI inflation on a rolling triennium. Funding is appropriated for future years at the rate of the CPI forecast plus 1%, and in the Budget preceding the relevant academic year funding rates are confirmed using a more up-to-date CPI forecast. The differential between the CPI increase and the appropriation is retained within the Vote for application elsewhere in the Student Component.

<b>Budget to be Charged (\$million)</b>	<b>2006/07</b>	<b>2007/08</b>	<b>2008/09</b>	<b>2009/10 and Outyears</b>
Budget 2006	29.1	59.2	59.2	59.2
Budget 2007		28.5	57.0	57.0

## Time-Limited Funding

Time-limited funding does not meet the definition of a “risk” under the PFA, 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 and may potentially be extended, using a \$5 million materiality threshold. They are often related to pilot programmes.

Vote	Description of Initiative	Operating Impact (\$million)
Biosecurity – Agriculture and Forestry	Painted Apple Moth eradication programme	6 in 2004/05
Communications	Digital Strategy – Information and Communications Technology capability, skills and development	18 from 2005/06 to 2008/09 (MYA)
Communications	Digital Strategy – high-speed connectivity for growth	20 from 2005/06 to 2008/09 (MYA)
Economic, Industry and Regional Development	Regional partnerships and facilitation for sustainable economic growth	57 from 2004/05 to 2006/07 (MYA)
Education	Microsoft software licensing	7 in 2004/05, 8 in 2005/06 and 4 in 2006/07
Energy	Electricity efficiency programme	1 in 2004/05, 8 in 2005/06 and 10 in 2006/07
Finance	Upgrade of rail network	200 from 2004/05 to 2007/08 (MYA)
Health	Meningococcal vaccine programme	106 in 2004/05, 31 in 2005/06 and 11 in 2006/07
Housing	Rural housing programme	8 in each of 2005/06, 2006/07 and 2007/08
Internal Affairs	Significant Community-Based Projects Fund	40 from 2005/06 to 2008/09 (MYA)
Police	Regional assistance mission Solomon Islands and Solomon Island executive support	7 in each of 2005/06 and 2006/07
Tourism	Tourism promotional budget targeting high-yield tourists	9 in 2005/06

The following table shows the impact on the operating balance if funding were to be appropriated to maintain funding levels for these initiatives (ie, extend the initiatives beyond their current scheduled completion dates). These amounts would need to be managed within the forecast operating spending.

Operating Impact (\$million)	2005/06	2006/07	2007/08	2008/09	2009/10 and Outyears
Funding to extend initiatives	6	15	70	104	119

## Quantified Risks

The risks outlined in these tables would, if they eventuated, impact on the Government's forecast new operating and/or capital spending amounts.

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

Quantified Risks as at 9 May 2005	Operating Balance	Gross Debt	Value of Risk (\$million)	Funding Received in Budget 2005 (\$million)
<b>New Risks</b>				
ACC – Public Health Acute	Decrease	Increase	16 from 2005/06	-
Culture and Heritage – Rugby World Cup 2011	Decrease	Increase	20 to 70 from 2005/06 to 2011/12	-
Economic Development – Improving Access to Finance	Decrease	Increase	Up to 2 operating and 40 capital over 5 years	-
Health – Health Emergency Preparedness Capability	Decrease	Increase	3 in 2005/06, 11 in 2006/07, 10 in 2007/08, and 9 from 2008/09	-
Transport – Harbour Link	-	Increase	35 in 2005/06	-
<b>Changed Risks</b>				
Child, Youth and Family Services – Residential Services Strategy 2003	Decrease	Increase	Operating of 8 in 2005/06 rising to 16.1 from 2009/10, and capital of 30 from 2005/06 to 2007/08	-
Corrections – Capital Projects	Decrease	Increase	92 operating and 118 capital in the forecast period	206 capital and 224 operating over the forecast period
Culture and Heritage – Public Broadcasting Programme of Action	Decrease	Increase	33.5 per annum	10.5m per annum
Education – School Property	-	Increase	136 capital in each of 2006/07, 2007/08 and 2008/09, and operating of 6 in 2006/07, 13 in 2007/08 and 20 from 2008/09.	77.5 capital in 2005/06, and operating of 3 in 2005/06 and 10 from 2006/07
Health – District Health Board deficits	Decrease	Increase	Up to 100 in 2005/06	-
Housing – Housing New Zealand Corporation's Long-Term Capital Requirements	-	Increase	1,600 over 10 years	25 in 2005/06, 65 in 2006/07, 20 in 2007/08 and 21 in 2008/09
Internal Affairs – 2004 Storms Response and Infrastructure Costs	Decrease	Increase	5 to 20 in 2005/06	No new funding in 2005 Budget, but 13 across 2003/04 and 2004/05

Quantified Risks as at 9 May 2005	Operating Balance	Gross Debt	Value of Risk (\$million)	Funding Received in Budget 2005 (\$million)
<b>Changed Risks – cont’d</b>				
Justice – New Supreme Court – Cost Escalation	-	Increase	15 to 20	-
New Zealand Defence Force – Defence – Capital Injections	-	Increase	589 from 2006/07 to 2010/11	410 capital in 2005/06
New Zealand Defence Force – Environmental Clean-up of Devonport Seabed Contamination	Decrease	Increase	13 over 2005/06 and 2006/07	-
Revenue – Further work on Business Taxation <ul style="list-style-type: none"> <li>• Fringe Benefit Tax Review</li> <li>• Subsidies for Payroll-Related Tax Compliance Costs</li> <li>• Tax and Depreciation</li> <li>• Taxation of Offshore Portfolio Investment and Intermediaries, including Superannuation</li> </ul>	Decrease	Increase	24 to 64 per annum 2 to 12 in 2005/06 and 7 to 45 from 2006/07 - 33 in 2006/07 and 130 from 2007/08	Elements of the Business Package relate to these items. The Business Package has a net cost of 229 in 2005/06, 229 in 2006/07, 105 in 2007/08 and 57 in 2008/09
<b>Unchanged Risks</b>				
Immigration – Immigration Policy	-	Increase	80 to 160 per annum	-
United Nations Convention on the Rights of the Child	Decrease	Increase	20 per annum	-

## Unquantified Risks

The risks outlined in these tables would, if they eventuated, impact on the Government's forecast new operating and/or capital spending amounts.

Unquantified Risks as at 9 May 2005	Operating Balance	Gross Debt	Funding Received in Budget 2005 (\$million)
<b>New Risks</b>			
Child, Youth and Family Services – Sustainable Service Delivery and Funding	Unclear	Unclear	-
Education – Reviews of Tertiary Education Expenditure	Unclear	Unclear	-
Tertiary Education Savings Scheme	Decrease	Increase	-
Transport – Regional Transport Initiatives	-	Increase	-
Transport – Wellington Transport Package	-	Increase	225 over 10 years
<b>Changed Risks</b>			
Education – Student Support	Decrease	Increase	10 in 2005/06, 14 in 2006/07, 16 in 2007/08, 17 in 2008/09 and outyears
Finance – Crown Overseas Properties	-	Increase	-
Fisheries – Māori Interest in Marine Farming	-	Increase	-
Housing – State Housing Project at Hobsonville	-	Increase	54 in 2005/06
Pay and Employment Equity Taskforce	Decrease	Increase	-
Social Development – Early Intervention	Decrease	Increase	37 in Budget 2005 with plans for more uncosted spending in Budget 2006
<b>Unchanged Risks</b>			
Education – Wananga Capital Injection	-	Increase	-
New Zealand Defence Force – Sale of Skyhawks and Aermacchi Trainers	-	Unclear	-
Social Development – Extending Opportunities to Work	Decrease	Increase	-
Social Development – Information Technology Systems	-	Increase	-
State Services Commission – State Sector Retirement Savings Scheme	Decrease	Increase	1.6 over 2004/05 to 2008/09 for operation of the scheme

## Risks removed since the *December Update*

The following risks have been removed since the *December Update*.

Expired Risks	Reason	Funding Received (\$million)
Agriculture and Forestry – Lower North Island Storm: On-farm Relief Measures	In forecasts	16 over 2004/05 and 2005/06
Education – Tertiary Education Funding Category Review	In forecasts	1 in 2005/06, 5 in 2006/07, -2 in 2007/08 and -13 in 2008/09
Environment – Climate Change	In forecasts and recognised as a contingent liability	Carbon charge revenue is forecast at 90 in 2006/07, 362 in 2007/08 and 359 in 2008/09
Foreign Affairs and Trade – Official Development Assistance	In forecasts	15 in 2005/06 and 63 from 2006/07
Health – Disability Support and Aged Care Services	In forecasts	49 in 2005/06 and 83 from 2006/07
Health – High and Complex Intellectual Disability Services	In forecasts	27 from 2004/05
Health – Orthopaedics	In forecasts	4 in 2005/06, 16 in 2006/07 and 27 from 2007/08
Health – Wage Bargaining	In forecasts	34 in 2004/05, 102 in 2005/06, and 149 from 2006/07
Holidays Act	In forecasts	53 from 2004/05
Internal Affairs – Review of Rates Rebate Scheme	In forecasts	50 from 2006/07
Lands and Conservation – Achievement of the Government's Objectives for the South Island High Country	In forecasts	40 in 2005/06 to 2007/08 and then 11 per annum in outyears
New Zealand Defence Force – Defence Capability and Resourcing Review	In forecasts	60 in 2005/06, 60 in 2006/07 and 67 from 2007/08
New Zealand Defence Force – Overseas Deployments	In forecasts	1 in 2004/05, 17 in 2005/06 and 5 in 2006/07
New Zealand Defence Force – Stand-alone Security Response Organisation	Included in DFP and Long-Term Development Plan	-
Research, Science and Technology – Health Research Package	In forecasts	13 in 2005/06, 19 in 2006/07 and 20 from 2007/08
Revenue – Amortisable Research and Development Expenditure	In forecasts	Included in the Business Package, which has a net cost of 229 in 2005/06, 229 in 2006/07, 105 in 2007/08 and 57 in 2008/09
Revenue – Exemption for Overseas Earnings	In forecasts	
Revenue – Tax Simplification for Small and Medium Enterprise	In forecasts	
Savings and Home Ownership	In forecasts	Operating of 10 in 2005/06, 99 in 2006/07, 291 in 2007/08, 154 in 2008/09 and 200 in outyears. Capital of 13 in 2005/06 and 15 in 2006/07
Transport – Toll Road Funding	In forecasts	100 in 2007/08 and 58 in 2008/09

## Statement of Fiscal Risks

### ***ACC – Public Health Acute (new, quantified risk)***

ACC funding for the provision of public health acute services for 2005/06 is currently being considered. The amount of additional funding to be paid by ACC has not yet been determined, but would decrease the operating balance by up to \$16 million in 2005/06 and outyears.

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

Source: Department of Labour

### ***Child, Youth and Family Services – Residential Services Strategy 2003 (changed, quantified risk)***

The Department of Child, Youth and Family Services has undertaken a comprehensive review of existing residential services and practices, including consideration of desired outcomes, a review of international good practice, and formal forecasting of demand. From this, the Department has developed a strategy for future residential services provision – the Residential Services Strategy 2003. The 2003 Strategy builds on the considerable investment in facilities made in implementing the 1996 Residential Services Strategy.

The Government has agreed in principle to fund the 2003 Strategy subject to fully developed and costed proposals. Some initiatives have already been agreed, and the remaining operating cost risk is \$8.4 million in 2005/06 rising to \$16.1 million in 2009/10 and outyears, which would decrease the operating balance. The remaining capital risk is \$29.5 million, which would increase gross debt. The current proposed phasing of this is \$4.4 million in 2005/06, \$7.4 million in 2006/07 and \$17.7 million in 2007/08.

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

Source: Department of Child, Youth and Family Services

### ***Child, Youth and Family Services – Sustainable Service Delivery and Funding (new, unquantified risk)***

The Government is reviewing the Department of Child, Youth and Family Services' funding requirements in order to identify options for sustainable levels of funding and service delivery in the medium term. Options may be submitted for consideration in Budget 2006. The risk is unquantified as it is unclear what change in departmental funding is required. Any change in funding to reflect a new baseline and/or meet necessary capital injections would impact on the operating balance and/or gross debt.

### ***Corrections – Capital Projects (changed, quantified risk)***

In Budget 2005, \$206 million capital and \$220 million operating was appropriated for Corrections capital projects. The Department of Corrections has estimated that a further total of \$118 million capital and \$92 million operating funding would be required over the forecasting period (with an ongoing operating cost of \$41 million from 2009/10) to meet future prison inmate forecasts.

The actual amounts depend on the specification and timing of the individual projects and the contracted prices. These estimates include consideration of funding for the Otago Men's Corrections Facility and Mt Eden Prison.

Capital injections would increase gross debt while operating funding would decrease the operating balance.

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

Source: Department of Corrections

***Culture and Heritage – Public Broadcasting Programme of Action (changed, quantified risk)***

On 3 February 2005, the Government released a Public Broadcasting Programme of Action. The Programme contains a set of priorities to guide public broadcasting policy over the next six years, and a series of proposals to give effect to these priorities. The Programme as a whole (if fully implemented) would have total ongoing operating costs rising to around \$44 million in 2009/10. Broadcasting initiatives of \$10.5 million per annum have been included in Budget 2005, leaving a remainder of around \$33.5 million. Other individual elements of the Programme of Action will be considered in future Budgets over the next six years. These would decrease the operating balance.

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

Source: Ministry for Culture and Heritage

***Culture and Heritage – Rugby World Cup 2011 (new, quantified risk)***

In May 2005, the New Zealand Rugby Union (NZRU) is likely to submit a bid to the International Rugby Board (IRB) to host the Rugby World Cup 2011 in New Zealand. The Government has agreed to provide the following direct financial support if the bid is successful: a \$20 million cash contribution, and an uncapped underwrite for the tournament on a 67:33 loss sharing basis (Government:NZRU). If the bid is successful, the operating balance could decrease by approximately \$20-70 million between 2005/06 and 2011/12.

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

Source: Ministry for Culture and Heritage

***Economic Development – Improving Access to Finance (new, quantified risk)***

The Government is considering options to improve firms' access to finance, including a new equity co-investment scheme. The amount of funding required would depend on the option chosen, if any. An equity co-investment scheme could require up to \$2 million operating and \$40 million capital spread over five or six years. This would decrease the operating balance and increase gross debt.

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

Source: Ministry of Economic Development.

***Education – Review of Tertiary Education Expenditure (new, unquantified risk)***

The Government is currently reviewing tertiary education spending with particular focus on sub-degree level tertiary spending where there has been large growth in participation and expenditure. Decisions are expected later in 2005 and may lead to changes in expenditure in 2006. The precise impact on the operating balance, if any, is unclear as it would depend on the outcome of the review.

***Education – School Property (changed, quantified risk)***

The Government has provided capital of \$77.5 million in 2005/06 for school accommodation. Additional capital injections for school accommodation are likely to be required in future years to meet roll growth. Additional capital injections could be up to \$136 million in each of the next three years with a corresponding increase in gross debt.

In addition to capital injections, consequential operating costs of \$6 million in 2006/07, \$13 million in 2007/08 and \$20 million in 2008/09 are likely to be incurred, which would decrease the operating balance.

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

Source: Ministry of Education

***Education – Student Support (changed, unquantified risk)***

The Government is considering a range of initiatives relating to student support. The initiatives under consideration include changes to student loan collection policy, student allowance payment rates, and any implications of the new universal benefit payment for student allowances. Depending on the initiatives selected this would decrease the operating balance.

***Education – Wananga Capital Injection (unchanged, unquantified risk)***

Ministers are currently negotiating with a Wananga (Māori tertiary education institution) 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, be provided funding to bring its facilities up to a standard comparable with other tertiary institutions and to meet additional capital requirements.

Any capital injection would increase gross debt. The fiscal risk is unquantified as disclosure could compromise the Crown in negotiations with the Wananga.

***Finance – Crown Overseas Properties (changed, unquantified risk)***

The Government is considering options relating to the continued use of certain Crown overseas properties.

The risk is unquantified as disclosure could compromise any negotiations the Crown may enter, but any additional operating funding would decrease the operating balance, and/or any additional capital funding would increase debt.

***Fisheries – Māori Interest in Marine Farming (changed, unquantified risk)***

The Māori Commercial Aquaculture Claims Settlement Act 2004 addresses Māori claims in commercial marine farming space from 21 September 1992 to 31 December 2004 (“pre-commencement space”) by providing iwi with 20% equivalent space. This obligation is to be met through three possible options: the provision of additional new space, or Crown purchase of existing farms from 2008, or provision of the financial equivalent of space from 2013.

Under the Act, any Māori claim relating to new aquaculture space after 31 December 2004 will be met by the provision of 20% of the new space.

To the extent that financial compensation or Crown purchase of existing farms is necessary to address Māori interests (as opposed to using new space), this would decrease the operating balance. The risk is unquantified as the amount or timing of any funding is unclear, and in addition, disclosure could compromise the Crown in negotiations with either commercial marine farm owners or iwi.

***Health – District Health Board Deficits (changed, quantified risk)***

Initial draft *District Annual Plans* from District Health Boards (DHBs) for 2005/06 indicate deficits in the order of \$100 million in 2005/06, primarily in Auckland, with smaller deficits in West Coast and Whanganui. A similar level of deficits is forecast for 2006/07. The Government has not accepted the size of these forecast deficits and is actively discussing actions and cost-containment measures with these DHBs.

The impact on the operating balance, if any, is unclear. Any deficits above that able to be funded from Vote Health would decrease the operating balance and/or increase gross debt. Specific potential pressures for DHBs include wage bargaining and funding for health of older people services.

This risk has changed since the 2004 DEFU to take into account the new financial forecasts submitted by DHBs.

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

Source: District Health Boards

***Health – Health Emergency Preparedness Capability (new, quantified risk)***

The Government is considering funding to address the capability and capacity of the health sector to respond to accidental or deliberate mass casualty emergencies, or a pandemic. This could cost up to \$3 million in 2005/06, \$11 million in 2006/07, \$10 million in 2007/08 and \$9 million in 2008/09 and outyears, which would decrease the operating balance.

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

Source: Ministry of Health

***Housing – HNZC’s Long-Term Capital Requirements (changed, quantified risk)***

The Government is currently considering Housing New Zealand Corporation’s (HNZC) long-term capital requirements in light of the demand for social housing and the need to reconfigure and modernise its housing stock. While some decisions were made in the 2005 Budget regarding the acquisition of new stock, the Government is likely to review acquisition targets and has still to consider options around modernisation programmes directed at existing stock. Decisions are likely in Budget 2006.

The Government is further examining the range of options and associated costs, with initial estimates of up to \$1.6 billion of capital costs over a 10- to 15-year horizon. Any new capital contributions would increase gross debt and would likely lead to an increase in the Income-Related Rent subsidy with a subsequent decrease in the operating balance.

***Housing – State Housing Project at Hobsonville (changed, unquantified risk)***

In Budget 2005, HNZC has received funding of \$54.3 million to acquire, under the Housing Act 1955, NZDF land at Hobsonville deemed surplus to defence requirements but suitable for state housing purposes. The Government may consider development options that would lead to the Crown giving additional capital to HNZC, which would increase gross debt.

***Immigration – Immigration Policy (unchanged, quantified risk)***

The Government has amended immigration investor policy. Migrants in the investor category will be required to invest \$2 million with the Government for five years. These bonds will be used to finance infrastructure. Migrants will receive a return on their investment based on inflation, and may withdraw up to half of the total investment after two years if they have a specific business proposal in New Zealand. The policy is to be implemented by 30 June 2005. Uptake of the new policy is unclear at this stage, and so has not been included in forecasts. The increase in gross debt, based on a flow of 40 to 80 people, is currently estimated to be between \$80 million and \$160 million per year.

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

Source: Department of Labour

***Internal Affairs – 2004 Storms Response and Infrastructure Costs (changed, quantified risk)***

The lower North Island and the Bay of Plenty were hit by severe storms during 2004. The Government reimburses some local authority costs under the National Civil Defence Plan. Several local authorities have made submissions for reimbursement, and further submissions are expected. The Government is working with local authorities to review the information provided and consider how to respond. The Government has already provided around \$13 million. Remaining costs could be between \$5 million and \$20 million and would reduce the operating balance.

Source: Department of Internal Affairs

***Justice – New Supreme Court – Cost Escalation (changed, quantified risk)***

In order to meet revised functional requirements, the Government is considering altering the 2003 design for accommodating the new Supreme Court. This could increase construction costs. The original scheme was approved by Cabinet at a cost of \$19 million; the additional capital cost could range from \$15 million to \$20 million, depending on the revised design option selected. This would increase gross debt.

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

Source: Ministry of Justice

***New Zealand Defence Force – Defence – Capital Injections (changed, quantified risk)***

Implementing the Government’s decisions on the future structure of the NZDF will involve a series of capital acquisitions across all three armed services and for HQNZDF to achieve the required capability upgrades. The Government has agreed to a capital injection of up to \$1.244 billion over 2001/02 to 2010/11. This has increased from the \$1 billion signalled in DEFU to provide \$35 million for additional Light Armoured Vehicle capability and \$209 million to extend the capital programme to address issues raised in the Defence Capability and Resourcing Review, including aligning some major weapons platforms with the Government’s intentions.

Of the Long-Term Development Plan funding, \$655 million has been agreed, leaving \$589 million remaining. 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.

Any capital injections would increase gross debt.

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

Source: New Zealand Defence Force

***New Zealand Defence Force – Environmental Clean-up of Devonport Seabed Contamination (changed, quantified risk)***

The Government has identified historic contamination in the seabed adjacent to the Calliope Dock at the Devonport Naval Base. Investigatory work on the contamination is underway, and it is anticipated that by mid-2005 better information will be available to determine the scope of the issue. Costs are estimated to be \$13.1 million over 2005/06 and 2006/07.

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

Source: New Zealand Defence Force

***New Zealand Defence Force – Sale of Skyhawks and Aermacchi trainers (unchanged, unquantified risk)***

As a result of the Government’s decisions on the future structure of the NZDF, NZDF is in the process of selling the Skyhawks and Aermacchi trainers. Proceeds from the sale would improve the operating balance.

This risk is unquantified as disclosure could compromise the Crown in the sale process.

### ***Pay and Employment Equity Taskforce (changed, unquantified risk)***

The Government has established the Pay and Employment Equity Unit in the Department of Labour to oversee the implementation of a five-year plan of action to establish pay and employment equity in the public service, public health and public education sectors. Until pay and employment equity audits and pay investigations have been undertaken in these sectors it is unclear what, if any, the fiscal implications of this process would be. However, any resulting increases in operating funding would decrease the operating balance.

### ***Revenue – Further Work on Business Taxation***

The Budget 2005 Business Package includes the following initiatives, some of which appeared as specific fiscal risks in the *December Update*:

<b>Budget Initiatives (\$million)</b>	<b>2005/06</b>	<b>2006/07</b>	<b>2007/08</b>	<b>2008/09</b>
<i>Financial Intermediaries</i> (involves alignment of the taxation of investment income from direct and indirect investments and modification to the taxation of offshore investment income)	-	-	120	100
<i>Depreciation</i> (includes adjustment of certain tax depreciation rates and an increase in the low-value asset write-off threshold)	219	276	260	222
<i>Fringe benefit tax</i> (includes lowering the fringe benefit valuation rate on motor vehicles and increasing the exemption thresholds for minor fringe benefits)	7	28	28	28
<i>Tax simplification</i> (involves aligning the payment dates for GST and provisional tax and allowing the payment of provisional tax on the basis of GST turnover)	-	-	46 <sup>1</sup>	53
<i>International recruitment</i> (a temporary tax exemption on foreign income will be made available to certain people who come to work here)	-	12	12	12
<i>Implementation costs</i>	3	4	1	1
Subtotal	229	320	467	416
Less: Carbon tax revenue	-	80	322	319
<b>Net Cost</b>	<b>229</b>	<b>239</b>	<b>145</b>	<b>97</b>

<sup>1</sup> There is also an impact on the operating balance occurring as a result of the deferral of the receipt of provisional tax payments by approximately two months. This deferral shifts \$760 million of tax revenue out of 2007/08.

Further work is still underway on the following four items in relation to taxation of business:

***Revenue – Fringe Benefit Tax review (changed, quantified risk)***

The Budget 2005 Business Package includes changes to fringe benefit tax policies. The Government is considering further work on changes to the fringe benefit tax rules focusing on eliminating certain anomalies in relation to motor vehicles.

The reduction in the operating balance would depend on which proposals are finally approved and the details of the legislation. However, the estimated net fiscal cost is likely to be within the range of \$24 million to \$64 million per annum.

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

Source: Inland Revenue

***Revenue – Subsidies for Payroll-Related Tax Compliance Costs (new, quantified risk)***

As part of the tax simplification programme the Government plans to implement a legislative framework to subsidise the use of payroll agents to meet small employers' PAYE obligations. The structure and amount of the subsidy are contingent on successful negotiation with payroll agents and the reduction in the operating balance will depend on the final structure of the subsidy adopted. However, the estimated cost of the subsidy is likely to be within the range of \$7 million to \$45 million per annum. On the basis that the subsidy can be negotiated, a target date of 1 April 2006 has been set for implementation.

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

Source: Inland Revenue

***Revenue – Tax and Depreciation (changed, unquantified risk)***

The Budget 2005 Business Package includes changes to depreciation policies. The Government is considering further issues related to depreciation, including the treatment of long-lived assets and potential changes to the tax treatment of rental housing in particular. However, the impact on the operating balance remains unclear as it would depend on the options chosen.

***Revenue – Taxation of Offshore Portfolio Investment and Intermediaries Including Superannuation (changed, quantified risk)***

The Budget 2005 Business Package includes changes to the taxation of domestic intermediaries and further work is underway. This includes consideration of the taxation of both onshore and offshore investments in equity by New Zealand residents. A target date of April 2007 has been set for implementation of changes, some of which have been included in the Budget 2005 Business Package. Further proposals are being considered and could cost an additional \$130 million, which would decrease the operating balance.

***Social Development – Early Intervention (changed, unquantified risk)***

Budget 2005 includes an initial investment of \$37.6 million over four years in early intervention services for children and families. Ministers are considering proposals for further development of the early intervention programme, including enhancements and expansion of the existing initiatives. New programmes may also be considered to respond better to the needs of children and their families.

Further proposals are still being developed, but any additional funding would decrease the operating balance.

***Social Development – Extending Opportunities to Work (unchanged, unquantified risk)***

Following on from Working for Families, the Government is considering options for simplifying the benefit system and reforming labour market assistance and service delivery in order to better support beneficiaries' entry to employment. Decisions are likely to be made as part of Budget 2006. The impact on the operating balance is unclear, as proposals are still being developed.

***Social Development – Information Technology Systems (unchanged, unquantified risk)***

The Government is considering the future development and/or replacement of its income benefit payment systems (SWIFTT and TRACE) and case management system. An Information Technology Strategy has been developed taking into account the Ministry's *Statement of Intent* and work on the future needs of the Ministry. Decisions will be made on development and/or replacement when appropriate concept and product evaluations have been completed.

The Ministry is seeking to fund any development and/or replacement from existing capital. To the extent the risk is not funded from the Department's balance sheet and existing baselines, the proposal would increase debt and reduce the operating balance.

***State Services Commission – State Sector Retirement Savings Scheme (unchanged, unquantified risk)***

The Government is considering options for extending the employer subsidy for members of the State Sector Retirement Savings Scheme beyond 3% (3% is the level of employer subsidy from 2005/06), and is also considering options for extending the scheme to the wider state sector.

The decrease in the operating balance would vary depending on the options chosen.

***Tertiary Education Savings Scheme (new, quantified risk)***

The Government is considering options for a Tertiary Education Savings Scheme. If the scheme does proceed the Government may include an upfront contribution as an incentive to encourage participation.

The decrease in the operating balance would vary depending on the options chosen.

***Transport – Harbour Link (new, quantified risk)***

The Government is considering a proposal of debt funding for the construction of a toll bridge over Tauranga harbour. The level of funding sought is approximately \$35 million in 2005/06. The capital cost of this would increase gross debt and any interest costs would decrease the operating balance.

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

Source: Ministry of Transport

***Transport – Regional Transport Initiatives (new, unquantified risk)***

The Government is considering possible involvement in regional transport initiatives working in participation with Local Government to make significant and timely improvements to regional land transport outcomes. A decision on a regional transport initiative for the Bay of Plenty is expected around June 2005.

***Transport – Wellington Transport Package (new, unquantified risk)***

The Government has agreed to funding of \$225 million over 10 years as part of the Wellington Transport Package. However, the Government has yet to consider the Western Corridor Transportation Study which is due to report at the end of May 2005. Costs for the Western Corridor could vary depending on the options chosen and may increase gross debt and/or decrease the operating balance.

***United Nations Convention on the Rights of the Child (unchanged, quantified risk)***

If unconditionally adopted, the United Nations Convention on the Rights of the Child would require New Zealand to confer the rights of the Convention on all children.

To date, New Zealand has reserved its right to distinguish between persons according to the nature of their authority to be in New Zealand. The Government established a review to consider whether this reservation can be removed. This could involve making changes to eligibility for some health, education and social services, which would decrease the operating balance by approximately \$20 million per annum. The review is due to report back in early 2005.

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

Source: The Treasury

## 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 2005, being the last set of published contingent liabilities.

Details of each of the following contingent liabilities can be accessed from the Treasury website at [www.treasury.govt.nz/forecasts/befu/2005](http://www.treasury.govt.nz/forecasts/befu/2005).

## Quantifiable Contingent Liabilities

<b>Guarantees and indemnities</b>	<b>Status<sup>12</sup></b>	<b>(\$ million)</b>
Cook Islands – Asian Development Bank loans	Changed	18
Indemnification of receivers and managers – Terralink Limited	Unchanged	10
Ministry of Justice – Treaty settlement, tax liabilities	Unchanged	76
Mighty River Power Limited – guaranteed payment obligations	Changed	17
Solid Energy New Zealand Limited	Changed	-
Ministry of Transport – funding guarantee	Unchanged	10
New Zealand Railways Corporation	Unchanged	10
Post Office Bank – guaranteed deposits	Unchanged	11
Guarantees and indemnities of SOEs and Crown entities	Changed	5
Other guarantees and indemnities	Changed	9
		<b>166</b>
<b>Uncalled capital</b>		
Asian Development Bank	Changed	1,046
European Bank for Reconstruction and Development	Unchanged	13
International Bank for Reconstruction and Development	Changed	1,159
		<b>2,218</b>
<b>Legal proceedings and disputes</b>		
Air New Zealand Limited – legal claim	Unchanged	107
Health – legal claims	Unchanged	104
Tax in dispute	Changed	408
Transpower New Zealand Limited	Unchanged	20
Other legal claims against SOEs and Crown entities	Changed	5
Other legal claims	Changed	83
		<b>727</b>
<b>Other quantifiable contingent liabilities</b>		
International finance organisations	Changed	1,252
Reserve Bank – demonetised currency	Unchanged	23
Social Development – claim for judicial review	Changed	52
Transpower New Zealand Limited	Unchanged	86
Other quantifiable contingent liabilities of SOEs and Crown entities	Changed	27
Other quantifiable contingent liabilities	Changed	18
		<b>1,458</b>
<b>Total quantifiable contingent liabilities</b>		<b>4,569</b>

<sup>12</sup> Relative to reporting in the 31 December 2004 *Crown Financial Statements*.

## Unquantifiable Contingent Liabilities

<b>Institutional guarantees</b>	<b>Status</b>
Asure New Zealand Limited	Unchanged
At Work Insurance Limited	Unchanged
Auckland rail lease	Unchanged
Bona Vacantia property	Unchanged
Crown research institutes	Unchanged
District Court Judges, Justices of the Peace, Coroners and Disputes Tribunal	Unchanged
District health boards – director indemnity (DHBs)	Unchanged
Earthquake Commission	Unchanged
Electricity Corporation of New Zealand Limited	Unchanged
Fisheries – indemnity provided for delivery of registry services	Unchanged
Fletcher Challenge Limited	Unchanged
Genesis Power Limited	Unchanged
Housing New Zealand Corporation	Unchanged
Indemnities against acts of war and terrorism	Unchanged
Maui Partners	Unchanged
National Provident Fund	Unchanged
New Zealand Railways Corporation	Unchanged
Persons exercising investigating powers	Unchanged
Ports of Auckland	Unchanged
Public Trust	Unchanged
Purchasers of Crown operations	Unchanged
Reserve Bank of New Zealand	Unchanged
State Insurance and Rural Bank – tax liabilities	Unchanged
Synfuels-Waitara Outfall Indemnity	Unchanged
Tainui Corporation	Unchanged
Toll NZ Limited – purchase of rail network assets	Unchanged
Works Civil Construction	Unchanged
Works Consultancy Services	Unchanged
<b>Other unquantifiable contingent liabilities</b>	
Abuse claims	New
Accident Compensation Corporation (ACC) litigations	Unchanged
Building Industry Authority litigation	Unchanged
Environmental liabilities	Unchanged
Genesis Power Limited	Unchanged
Kyoto Protocol	Changed
Sale of Crown assets	Unchanged
Treaty of Waitangi claims	Unchanged
Treaty of Waitangi claims – settlement relativity payments	Unchanged