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Specific Fiscal Risks

Introduction

This chapter describes the specific fiscal risks to the Crown, including contingent liabilities. The Fiscal Responsibility Act (FRA) 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 FRA:

- *Reasonable certainty criteria* – risks have not been included in the fiscal forecasts because they reflect government decisions or legislative commitments with uncertain fiscal consequences or timing.
- *Materiality criteria* – 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 criteria* – 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 FRA 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.

Time-Limited Funding

Time-limited funding does not meet the definition of a "risk" under the FRA, 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 initiatives (ie, extend the initiative beyond its current scheduled completion date), the total impact would be up to $28 million in 2005/06 and $35 million from 2006/07, which would need to be managed within the forecast operating spending amounts.

Vote	Description of initiative	Operating impact ($ million)
Agriculture and Forestry	Sustainable Farming Fund	10 from 2006/07
Defence Force	New Zealand Defence Force contribution to Operation Enduring Freedom	7 from 2005/06
Defence Force	Provincial Reconstruction Team to Afghanistan	16 in 2005/06, 20 from 2006/07
Education	Microsoft Software Licensing	5 in 2006/07, 9 from 2007/08
Housing	Rural Housing Programme	5 in 2005/06, 2006/07, 2007/08

Statement of Specific Fiscal Risks

The tables below summarise fiscal risks as at 7 May 2004.

Quantified Risks[9]

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

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

Risks as at 7 May 2004	Operating balance/net worth	Gross debt[10]	($ million)
New risks			
Health – Orthopaedics	Decrease	Increase	-18 operating in 2005/06, -25 in 2006/07, -30 in 2007/08
Health and ACC – Public Health Acute Services	Decrease	Increase	-32 operating in 2004/05, -8 operating in outyears
Internal Affairs – Weathertight Homes Resolution Service	Decrease	Increase	-25 from 2005/06
Lands – Surplus Government Property Sales	N/A	Decrease	12 capital in 2004/05
Transfer of Westhaven and Hobson West Marinas to Auckland City Council	Decrease	Decrease	46 capital
Changed risks			
Child, Youth and Family Services – Residential Services Strategy 2003	Decrease	Increase	-7 operating in 2004/05 rising to -26 in 2007/08 -27 capital in each of 2006/07 and 2007/08
Corrections – Capital Projects	Decrease	Increase	-309 capital and -153 operating over 4 years

Notes:

9 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.

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

Risks as at 7 May 2004	Operating balance/net worth	Gross debt[10]	($ million)
Education – School Property	Decrease	Increase	-55 capital in 2004/05, -125 in 2005/06; -125 in 2006/07, -125 in 2007/08 -1 operating in 2004/05, -3 in 2005/06, -7 in 2006/07, -12 in 2007/08
Immigration – Immigration Policy	Decrease	Increase	-200 to -500 operating in 2004/05
New Zealand Defence Force – Stand-Alone Security Response Organisation	Decrease	Increase	-6 operating in 2005/06, -7 in 2006/07 and outyears, -21 capital in 2005/06
Tourism – Support for Team New Zealand for 2007 America's Cup	Decrease	Increase	-28 operating over 2004/05 to 2006/07
United Nations Convention on the Rights of the Child	Decrease	Increase	-20 operating from 2004/05
Unchanged risks			
Customs – Container Security	Decrease	Increase	-20 operating from 2004/05
New Zealand Defence Force – Defence – Capital Injections	Decrease	Increase	-749 capital from 2004/05
New Zealand Defence Force – Environmental Clean-ups of Defence Bases	Decrease	Increase	-10 operating in 2005/06, -5 in 2006/07
Revenue – Exemption for Overseas Earnings	Decrease	Increase	-20 operating from 2005/06
Revenue – Tax Simplification for Small and Medium Enterprises	Decrease	Increase	-20 to -40 operating from 2005/06

Unquantified Risks

The risks outlined in this table would, if they eventuate, impact on the Government's forecast new operating and capital spending amounts.

Risks as at 7 May 2004	Operating balance/ net worth	Gross debt
New risks		
Energy – Gas Exploration	Unclear	Unclear
Holidays Act 2003	Decrease	Increase
Housing – Housing New Zealand Corporation's Long-term Capital Requirements	Decrease	Increase
Infrastructure Projects (Funded by Infrastructure Bonds)	Unclear	Unclear
Internal Affairs and Agriculture and Forestry – Lower North Island Storms	Decrease	Increase
Justice – Ministry of Justice Baseline Review	Decrease	Increase
New Zealand Defence Force – Defence Capability and Resourcing Review	Decrease	Increase
Reserve Bank – Foreign Exchange Reserves	N/A	Increase
Revenue – Issues Paper on Depreciation	Decrease	Increase
Revenue – Review of Tax Laws Applying to the Banking Sector	Unclear	Unclear
Tertiary Education Funding Category Review	Unclear	Unclear
Changed risks		
Environment – Climate Change	Unclear	Unclear
Health – District Health Board Deficits	Unclear	Unclear
Health – Wage Bargaining	Decrease	Increase
Pay and Employment Equity Taskforce	Decrease	Increase
Revenue – Changes to the Paid Parental Leave Scheme	Decrease	Increase
Revenue – Taxation of Offshore Portfolio Investment/Taxation of Intermediaries	Unclear	Unclear
Unchanged risks		
Air New Zealand	Unclear	Unclear
Education – Collective Employment Agreements	Decrease	Increase
Education – Partnerships for Excellence	Potentially increase	Increase
Education – Wānanga Capital Injection	N/A	Increase

Risks as at 7 May 2004	Operating balance/ net worth	Gross debt
Finance – Crown Overseas Properties	Unclear	Unclear
Health – Refinancing of District Health Board Private Debt	N/A	Increase
Housing – State Housing Project at Hobsonville	N/A	Increase
Lands and Conservation – Achievement of the Government's Objectives for the South Island High Country	Decrease	Increase
Maui Gas Supply	Decrease	Increase
New Zealand Defence Force – Relocation of NZDF Headquarters	Unclear	Unclear
New Zealand Defence Force – Sale of Skyhawks and Aermacchi Trainers	Increase	Decrease
Revenue – Fringe Benefit Tax Review	Unclear	Unclear
Revenue – Gaming Review	Unclear	Unclear
Revenue – Taxation of Savings and Investment Vehicles, Including Superannuation Funds	Unclear	Unclear
Social Development – Benefit Payment Information Technology Systems	Decrease	Increase
State-Owned Enterprise Capital Injections	N/A	Increase

Risks Removed Since the 2003 *December Update*

Risks	Comment
ACC – Medical Misadventure Review	In baselines
ACC – Treatment Costs	In baselines
Corrections – Funding of Staff Pay Settlements	In baselines
Customs – Enhanced Border Management	In baselines
Education – Early Childhood Education Strategic Plan	In baselines
Education – Student Support	In baselines
Foreign Affairs and Trade – Overseas Development Assistance	In baselines
Health – Extension of the Health Capital Envelope	In baselines
Health – Extension of the Health Funding Path	In baselines
Health – Mental Health Blueprint	In baselines
Health – Quality and Safety	In baselines
Housing – Housing Strategy	Does not meet criteria for disclosure
Justice – Courts Capability	In baselines
New Zealand Defence Force – RNZAF – Pay and Allowances	In baselines
New Zealand Defence Force – RNZAF – Personnel Increases	In baselines
Police – Capital Projects	In baselines
Social Development – Future Directions	In baselines
State Services – Electronic Authentication	In baselines
Transport – Auckland Transport	In baselines

Statement of Fiscal Risks

Air New Zealand (unchanged, unquantified 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) have rejected the proposed alliance, as the authorities could not be satisfied that the public benefits from the proposed alliance would outweigh the detriment, but the airlines are appealing these decisions in both countries.

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.

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 – 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 $7 million in 2004/05 rising to $26 million in 2007/08 and outyears, which would decrease the operating balance ($13 million rising to $31 million in the *December Update*). The remaining capital risk is $27 million in each of 2006/07 and 2007/08, which would increase gross debt.

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

Source: Department of Child, Youth and Family Services

Corrections – Capital Projects (changed, quantified risk)

The Department of Corrections has estimated that a total of $309 million of capital injections and operating funding of $153 million will be required over the forecasting period for capital projects to meet future prison muster forecasts ($393 million of capital injections and operating funding of $126 million in the *December Update*).

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.

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

Source: Department of Corrections

Customs – Container Security (unchanged, quantified 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, but is considering fees to be imposed on exporters, importers and transport operators.

The ongoing operating cost is expected to be up to $20 million in 2004/05 and outyears, which would decrease the operating balance depending on the level of cost recovery.

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

Source: New Zealand Customs Service

Education – Collective Employment Agreements (unchanged, unquantified risk)

All primary and secondary school principals' and teachers' collective agreements will have expired by 30 June 2004. The Government will need to meet any fiscal impact in 2004/05 and beyond due to the renegotiation of these agreements, and any adjustments to individual agreements. Any increase in funding will decrease the operating balance.

This risk is unquantified, as disclosure could compromise the Crown in negotiations.

Education – Partnerships for Excellence (unchanged, unquantified risk)

The Government has decided to establish an arrangement called "Partnerships for Excellence" whereby the Government matches private sector investment in the tertiary sector. The Government is currently considering a number of applications for partnerships. This risk is unquantified as funds will be considered on an annual basis subject to budgetary pressures.

Education – School Property (changed, quantified risk)

The Government has provided $46 million in 2004/05 for school accommodation. Additional capital injections for school accommodation are likely to be required later in 2004/05 and in future years to meet roll growth. Capital injections are estimated to be up to $55 million in 2004/05, $125 million in 2005/06, $125 million in 2006/07, and $125 million in 2007/08 ($115 million per annum in the *December Update*).

In addition to capital injections, consequential operating costs of $1 million in 2004/05, $3 million in 2005/06, $7 million in 2006/07 and $12 million in 2007/08 are likely to be incurred with each outyear's capital injection ($8 million, $21 million and $30 million in the *December Update*).

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

Source: Ministry of Education

Education – Wānanga Capital Injection (unchanged, unquantified risk)

Ministers are currently negotiating with one wānanga (Māori tertiary institution) over settlement of its Waitangi Tribunal claim. The Waitangi Tribunal has recommended that the wānanga be compensated for capital expenditure that has been incurred on facilities to date, and be provided funding to bring its facilities up to a standard comparable with other tertiary education institutions and to meet additional capital requirements.

There is also a possibility that the Government may have to provide a further capital injection for a wānanga in accordance with the conditions of an existing settlement.

The fiscal risk is unquantified as disclosure could compromise the Crown in negotiations.

Energy – Gas Exploration (new, unquantified risk)

The Government is considering a package of proposals to promote gas exploration in New Zealand. The details and size of the package are still under development. Any costs of the package would decrease the operating balance.

Environment – Climate Change (changed, unquantified risk)

The Government is implementing a policy package to meet New Zealand's greenhouse gas emission reduction commitments under the Kyoto Protocol. However, the future of the Protocol is uncertain, because it is dependent on Russia's ratification.

If the Protocol does not proceed, the Government will review all Kyoto-dependent policies, the impact of which on the operating balance is uncertain.

A further risk is that of New Zealand's net emissions position at the end of the First Commitment Period. Should a net deficit eventuate, this would pose a fiscal liability to the Crown.

The Government has also proposed implementing a charge on greenhouse gas emissions. Negotiated greenhouse gas agreements are underway for liable firms deemed to have "competitiveness at risk" by the introduction of this charge. The proposed charge would include revenue recycling to return revenue from the charge to taxpayers. The net impact of the charge on the operating balance is at present unclear.

This risk has changed since the *December Update* to reflect ongoing policy development.

Finance – Crown Overseas Properties (unchanged, 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 will decrease the operating balance, while capital funding would increase gross debt. Alternatively, the sale of any properties would decrease gross debt.

Health – District Health Board Deficits (changed, unquantified risk)

Initial draft *District Annual Plans* from district health boards (DHBs) for 2004/05 indicate deficits of $55 million in 2004/05 and $49 million in 2005/06. 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 the health funding allocation will decrease the operating balance and increase gross debt.

This has changed since the *December Update* to take into account the new deficit forecasts submitted by DHBs.

Source: Ministry of Health

Health – Orthopaedics (new, quantified risk)

The Government has committed to funding part of the cost of increasing the intervention rate for orthopaedic surgery from underspends in existing Health appropriations. The actual source of this funding within the Vote has yet to be determined. If these costs are not met from within Vote Health they will need to be funded from the Government's forecast new operating spending amounts. This would decrease the operating balance by $18 million in 2005/06, $25 million in 2006/07 and $30 million in 2007/08.

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

Source: Ministry of Health

Health – Refinancing of District Health Board Private Debt (unchanged, unquantified risk)

The Government is considering refinancing DHB private sector debt earlier than previously forecast. All DHB debt owed to private lenders is currently being refinanced with debt supplied by the Crown. Private debt is usually refinanced upon maturity of the existing facility, but an opportunity may arise for a DHB to refinance earlier than forecast to take advantage of the lower interest cost charged by the Crown.

If the Government decides to refinance debt earlier than originally forecast this would increase gross debt. This is a timing change and would reduce the requirement for refinancing in years beyond the current forecasting period.

Health – Wage Bargaining (changed, unquantified risk)

Upcoming bargaining rounds in the health sector could result in significant increases in wage costs. If this cost is not met within DHBs' funding paths or the three-year Health Funding Package it would decrease the operating balance or increase gross debt (via DHB deficits). This risk has been updated since the *December Update* to reflect new information.

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

Health and ACC – Public Health Acute Services (new, quantified risk)

The Government is considering issues around the calculation and payment of this funding. The final costs of both past-year reconciliations and the implications for future funding streams have yet to be determined but would decrease the operating balance by up to $32 million in 2004/05, and up to $8 million from 2005/06.

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

Sources: Ministry of Health and ACC

Holidays Act 2003 (new, unquantified risk)

The Holidays Act 2003 makes a number of changes that will have fiscal implications for the public sector. If these costs are not met within agency baselines or sector-specific funding packages, they will decrease the operating balance.

Housing – HNZC's Long-Term Capital Requirements (new, unquantified risk)

The Government is currently considering Housing New Zealand Corporation's (HNZC's) long-term capital requirements in light of the demand for social housing and the need to reconfigure and modernise its housing stock. The Government will consider a number of scenarios of what may be required over the next 12 months.

The risk is unquantified as the nature of demand for social housing and appropriate responses have not yet been finalised. However, any new capital injections would increase gross debt and would lead to an increase in the income-related-rent subsidy with a subsequent decrease in the operating balance.

Housing – State Housing Project at Hobsonville (unchanged, unquantified 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. Land made available for purchase by the NZDF was acquired by HNZC at the end of 2002/03. Additional land is expected to become available over the next three to four years.

Depending on development options taken and timing, HNZC may require additional capital from the Government, which would increase gross debt.

Infrastructure Projects (funded by infrastructure bonds) (new, unquantified risk)

The Minister of Finance has instructed the Treasury to investigate the potential for introducing a new bond (an infrastructure bond) to assist in the direct financing of specific infrastructure projects. The fiscal impact of such infrastructure projects is unclear as it will depend on the particular projects and how they will be financed.

Immigration – Immigration Policy (changed, quantified risk)

The Government has made some high-level decisions about policy changes to the Investor category and is presently considering a number of implementation issues. The impacts on the fiscal aggregates are unclear. However, there is an intention for some migrants to provide investment finance to the Government that will then be targeted towards specific areas of government expenditure. The funds will be repayable to migrants after a specified time period, and such repayment is intended to be financed through future migrant investment. This policy is likely to be implemented during 2004/05, with an impact in the range of $200 million to $ 500 million, which would decrease the operating balance and increase gross debt.

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

Sources: New Zealand Immigration Service and Department of Labour

Internal Affairs – Weathertight Homes Resolution Service (new, quantified risk)

The Department of Internal Affairs runs the Weathertight Homes Resolution Service. The Service may continue to process claims beyond June 2005. The costs of continuing the service will depend on the volume of claims received, but could be up to $25 million per annum from 2005/06.

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

Source: Department of Internal Affairs

Internal Affairs and Agriculture and Forestry – Lower North Island Storms (new, unquantified risk)

The lower North Island was hit by severe storms in February 2004. The Government reimburses some local authority costs under the *National Civil Defence Plan* and 10 local authorities have provided a combined submission for $32 million, and have indicated that they may seek funding above this amount later. The Government is reviewing the information provided and is considering how to respond.

In addition, the Government has approved $25 million for on-farm relief measures. There is a risk that further funding may be required for this initiative.

The final cost of both risks remains unquantified at this stage.

Sources: Department of Internal Affairs and Ministry of Agriculture and Forestry

Justice – Ministry of Justice Baseline Review (new, unquantified risk)

The Government is reviewing the Ministry of Justice's funding requirements in order to provide sustainable funding levels and service delivery in the medium term. This risk is unquantified as the amount of any change in departmental funding is unclear, but any increase in funding to meet additional operating and capital costs would decrease the operating balance and increase gross debt.

Lands – Surplus Government Property Sales (new, quantified risk)

The Government is considering selling high-value properties, and these sales could become unconditional before June 2004. These sale proceeds would decrease gross debt by up to $12 million.

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

Source: Land Information New Zealand

Lands and Conservation – Achievement of the Government's Objectives for the South Island High Country (unchanged, unquantified risk)

In 2003 the Government agreed a set of objectives for the South Island high country. It is now considering options to achieve and fund these objectives, including the Land Tenure Reform process. This analysis is still being undertaken and decisions are expected in the 2005 Budget.

The risk is unquantified as disclosure could compromise the Crown in negotiations, but any increase in funding would decrease the operating balance and any new capital injections would increase gross debt.

Maui Gas Supply (unchanged, unquantified risk)

The Government is considering options to improve certainty of Maui 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.

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

Implementing the Government's decisions on the future force structure of the 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 $251 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. Projects include Project Protector, which includes the purchase of several new vessels at a cost of around $492 million over the next five years and yet to be quantified operating costs. Any capital injections would increase gross debt.

Source: New Zealand Defence Force

New Zealand Defence Force – Defence Capability and Resourcing Review (new, unquantified risk)

The Government has agreed to capital injections to the NZDF (as outlined above). When these injections are made, there will be associated operating costs to ensure the equipment procured can be introduced effectively into service, maintained and operated with the right number of appropriately trained personnel and have the relevant funding provided for the costs of depreciation. Additional operating funding pressures are possible with changing operational tempo and the introduction of new capabilities. The

Government is considering a Defence Capability and Resourcing Review to assess these issues and the impacts they have on the medium to longer-term needs of the NZDF.

This risk is unquantified as it is uncertain what the review outcomes will be.

New Zealand Defence Force – Environmental Clean-ups of Defence Bases (unchanged, quantified risk)

The Government is considering the options for dealing with areas of historic contamination at several NZDF bases, including the seabed adjacent to the Calliope Dock at the Devonport Naval Base. The estimated cost of cleaning up identified areas is $10 million in 2005/06 and $5 million in 2006/07 which would decrease the operating balance.

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

Source: New Zealand Defence Force

New Zealand Defence Force – Relocation of NZDF Headquarters (unchanged, unquantified risk)

The NZDF's current leases expire between 2004 and 2006, with the primary location at Stout Street needing to be vacated by March 2006. The NZDF is in negotiations with Capital Properties to consolidate all accommodation requirements for the NZDF, Ministry of Defence and New Zealand Security Intelligence Service. The Government is considering the options for the term of the lease and the rental mechanisms that will apply.

The risk is unquantified as disclosure could compromise the Crown in negotiations.

New Zealand Defence Force – Sale of Skyhawks and Aermacchi Trainers (unchanged, unquantified 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.

Source: New Zealand Defence Force

New Zealand Defence Force – Stand-Alone Security Response Organisation (changed, quantified risk)

New Zealand's ability to respond to chemical, biological, radiological and explosive threats has been under review since 2001. The 2002 Budget provided some funding for the establishment of a national chemical and biological response capability. The Government is considering proposals for a more comprehensive and responsive approach to deal with these threats. The estimated operating costs of a stand-alone security response organisation are $6 million in 2005/06 and $7 million in 2006/07 and outyears, which would decrease the operating balance, and capital costs of $21 million in 2005/06 only, which would increase gross debt. These costs impact a year later than anticipated in the *December Update*.

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

Source: New Zealand Defence Force

Pay and Employment Equity Taskforce (changed, unquantified risk)

The Government is considering proposals from the Pay and Employment Equity Taskforce that will have an impact on issues of pay and employment equity in the public service, public health and education sectors. Given the uncertainty around the timing and nature of any initiatives that may arise from these proposals and the extent to which they could be funded within baselines, it is not possible to determine the fiscal cost. However, any increased operating funding would decrease the operating balance.

This risk has changed since the *December Update* to reflect the fact that the Government is now considering specific proposals, rather than awaiting a report from the Taskforce.

Reserve Bank – Foreign Exchange Reserves (new, unquantified risk)

The Reserve Bank has the capacity to intervene in the foreign exchange market for the purpose of reducing variability in the exchange rate cycle, where doing so would be consistent with maintaining medium-term price stability. The Reserve Bank may seek additional reserves funding to enable it to intervene.

This risk is unquantified as disclosure would compromise the economic interests of the Crown.

Revenue – Changes to the Paid Parental Leave Scheme (changed, unquantified risk)

The Government has announced an extension of the paid parental leave scheme from 1 December 2004. The Government is considering further changes to the paid parental leave scheme to increase access to leave around the birth or adoption of a child for employed parents who do not meet the current criteria.

The impact on the operating balance will depend on the changes chosen.

Revenue – Exemption for Overseas Earnings (unchanged, quantified risk)

The Government is considering options to reduce the tax-related costs for businesses of recruiting overseas workers.

The Government has released a discussion document proposing a time-limited exemption from tax on some or all overseas investment income, for people coming to work as employees in New Zealand. However, any proposal is not expected to be implemented before 2005/06.

The impact of this proposal on the operating balance is likely to be in the order of $20 million per annum, however the final impact remains unclear as it depends on the options chosen.

Source: Inland Revenue

Revenue – Fringe Benefit Tax Review (unchanged, unquantified 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. A discussion document on this issue was released in December 2003. Any legislative changes resulting from the review will be introduced in 2004/05.

Any impact on the operating balance from any legislative amendments is unclear at this stage.

Revenue – Gaming Review (unchanged, unquantified risk)

The Gaming Review was completed and the Gambling Act has now been passed. The Government, however, is still considering the taxation of gaming. Any impact on the operating balance arising from a response, whether positive or negative, is unclear.

Revenue – Issues Paper on Depreciation (new, unquantified risk)

The Government is considering issues related to depreciation, including the overall structure of depreciation, the detailed application of depreciation to specific types of assets, and the particular treatment of rental housing.

The impact of any specific proposal(s) that might emerge from this work would vary widely depending on the options chosen and the design and implementation of those options.

Revenue – Review of Tax Laws Applying to the Banking Sector (new, unquantified risk)

The Government is reviewing the tax laws applying to the banking sector to ensure that they are robust and that an appropriate level of tax is paid on New Zealand banking income. The impact on the operating balance would depend on which measures are implemented.

Revenue – Tax Simplification for Small and Medium Enterprises (unchanged, quantified risk)

The Government released a discussion document in September 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 2005/06, which would decrease the operating balance.

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

Source: Inland Revenue

Revenue – Taxation of Offshore Portfolio Investment/Taxation of Intermediaries (changed, unquantified risk)

The Government released an issues paper at the end of last year on reforms to the tax rules for offshore portfolio investment in equity. This paper contained options for reform. Submissions on the paper highlighted issues arising from the offshore/onshore boundary. As a result a programme of work looking at taxation of domestic intermediaries (which invest onshore and offshore) has commenced since the *December Update*. This risk has widened as the taxation of both onshore and offshore investment, in equity and shares, by New Zealand residents is now under consideration. A target date of April 2006 has been set for implementation of changes.

Revenue – Taxation of Savings and Investment Vehicles, Including Superannuation Funds (unchanged, unquantified risk)

The Government is broadly considering whether the tax system creates impediments to adequate saving, whether savings intermediaries are correctly taxed, 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.

Social Development – Benefit Payment 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). Decisions will be made when an information technology 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.

The Ministry is attempting to fund any development from existing capital. Depending on what decisions are made, any future capital injections for development costs will increase gross debt, and operating funding will increase the operating balance. The quantum of the risk cannot be determined until decisions have been made about which options are to be chosen.

State-Owned Enterprise Capital Injections (unchanged, unquantified risk)

The Government is considering providing additional capital injections to SOEs, subject to there being favourable investment proposals available that would warrant an injection of equity. Proposals to provide additional Crown equity will be considered on a case-by-case basis.

This risk is unquantified because the Minister of Finance has yet to fully consider the quantum of any additional equity to be provided to SOEs, and also because disclosure of amounts in relation to any specific proposal from an SOE could compromise the Crown in commercial activities.

Tertiary Education Funding Category Review (new, unquantified risk)

The Government has agreed to a Funding Category Review that will seek to address anomalies in student component funding rates, and decisions are likely to be made by the end of 2004. The Government has indicated that additional funding will be made available for implementing the results of the Review. The impact, if any, of this proposal on the operating balance or debt is unclear as it depends on the options chosen.

This risk is unquantified as disclosure would compromise the economic interests of the Crown.

Tourism – Support for Team New Zealand for 2007 America's Cup (changed, quantified risk)

The Government has announced that it has initially committed $6 million to Team New Zealand to retain team members for the 2007 America's Cup in Spain.

The Government is considering up to a further $28 million for sponsoring Team New Zealand between 2004/05 and 2006/07, contingent on Team New Zealand raising $2 of sponsorship for every $1 of Government funding.

Transfer of Westhaven and Hobson West Marinas to Auckland City Council (new, quantified risk)

The Government recently agreed to acquire the Westhaven and Hobson West marinas for approximately $54 million, and has proposed that these two marinas be transferred to Auckland City Council for approximately $46 million.

Auckland City Council is undertaking a Special Consultative Procedure in accordance with the Local Government Act 2002 before deciding whether or not to acquire the two marinas. Auckland City Council has not yet made its decision, but should it decide to make the purchase, the payment would decrease gross debt.

Source: The Treasury

United Nations Convention on the Rights of the Child (changed, 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.

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, education and social services, which may decrease the operating balance by approximately $20 million per year ($14 million in the *December Update*).

This risk has been updated to reflect the estimated cost of previously unforeseen risks associated with lifting the reservation.

The Minister of Finance has yet to fully consider 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 2004, 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/befu/2004.

Quantifiable Contingent Liabilities

Guarantees and indemnities	Status[11]	($ million)
Cook Islands – Asian Development Bank loans	Unchanged	17
Indemnification of receivers and managers – Terralink Limited	Unchanged	10
Indemnification of touring exhibitions	Changed	51
Ministry of Justice – Treaty settlement, tax liabilities	New	93
Mighty River Power Limited – guaranteed payment obligations	Unchanged	50
Ministry of Transport – funding guarantee	Unchanged	10
Post Office Bank – guaranteed deposits	Changed	12
Guarantees and indemnities of SOEs and Crown entities	Changed	4
Other guarantees and indemnities	Changed	2
		249
Uncalled capital		
Asian Development Bank	Changed	1,070
European Bank for Reconstruction and Development	Unchanged	13
International Bank for Reconstruction and Development	Changed	1,241
		2,324
Legal proceedings and disputes		
Air New Zealand Limited – legal claim	New	107
Health – legal claims	Unchanged	104
Tax in dispute	Changed	345
Legal proceedings and disputes of SOEs and Crown entities	Changed	9
Other legal claims	Changed	88
		653
Other quantifiable contingent liabilities		
International finance organisations	Changed	846
Reserve Bank – demonetised currency	Unchanged	23
Social Development – claim for judicial review	Changed	72
Transpower New Zealand Limited – other quantifiable contingent liabilities	Unchanged	54
Other quantifiable contingent liabilities of SOEs and Crown entities	Changed	40
Other quantifiable contingent liabilities	Changed	41
		1,076
Total quantifiable contingent liabilities		**4,302**

[11] Relative to reporting in the 31 December 2003 Crown financial statements.

Unquantifiable Contingent Liabilities

Institutional guarantees	**Status**
Asure New Zealand Limited	Unchanged
At Work Insurance Limited	Unchanged
Auckland rail lease	Unchanged
Building Industry Authority	New
Crown research institutes	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
Ministry of Fisheries – indemnity provided for delivery of registry services	Unchanged
Housing New Zealand Corporation	Unchanged
Indemnities against acts of war and terrorism	Unchanged
Maui Partners	Unchanged
National Provident Fund	Changed
New Zealand Railways Corporation	Unchanged
Persons exercising investigating powers	Unchanged
Public Trust	Unchanged
Purchasers of Crown operations	Unchanged
Reserve Bank of New Zealand	Unchanged
State Insurance and Rural Bank – tax liabilities	Unchanged
Transpower New Zealand	Changed
Works Civil Construction	Unchanged
Works Consultancy Services	Unchanged
Other unquantifiable contingent liabilities	
Environmental liabilities	Changed
Genesis Power Limited	Unchanged
New Zealand Educational Institute	New
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