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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 $529 million in 2004/05, $86 million in 2005/06 and $47 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	25 in 04/05, 11 in 06/07
Agriculture and Forestry	Response to Lower North Island storm	23 in 04/05
Agriculture and Forestry	Response to Bay of Plenty storm	6 in 04/05
Biosecurity – Agriculture and Forestry	Painted Apple Moth eradication programme	6 in 04/05
Defence Force	Engineering Deployment in Afghanistan	20 in 04/05
Defence Force	Accommodation – New Zealand Defence Force	5 in 06/07
Education	Project PROBE	29 in 04/05
Education	Microsoft Software Licensing	8 in 04/05, 9 from 05/06, 4 from 06/07
Energy	Electricity Efficiency Programme	8 in 05/06, 11 from 06/07
Finance	Upgrade of Rail Network	200 from 04/05 to 07/08 (MYA)
Health	Meningococcal Vaccine Programme	94 in 04/05, 47 from 05/06, 12 from 06/07
Immigration	GIF – targeting skills in Immigration	11 in 04/05 and 05/06, 4 from 06/07
Internal Affairs	Weathertight Homes Resolution Service	18 in 04/05
Internal Affairs	Chinese Poll Tax Reconciliation Trust	5 in 04/05
Lands	Land Tenure Reform programme	57 in 04/05
Social Development	Alternatives to physical punishment	6 in 04/05
Social Development	Future Directions	21 in 04/05, 11 from 05/06

Quantified Risks

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 2 December 2004	Operating balance/net worth	Gross Debt	($million)
New Risks			
Culture and Heritage – Public Broadcasting Programme of Action	Decrease	Increase	-10 operating in 2005/06 rising to -50 in 2009/10 and outyears
Justice – New Supreme Court – Cost Escalation	n/a	Increase	from -9 to -25 capital
New Zealand Defence Force – Project Protector	Decrease	Increase	-5 operating in 2005/06 rising to -$68 in 2008/09 and outyears
Research, Science and Technology – Health Research Package	Decrease	Increase	-22 operating in 2005/06 rising to -39 in 2007/08 and outyears
Social Development – Early Intervention	Decrease	Increase	-28 in 2005/06 rising to -57 in 2006/07 and outyears
Changed Risks			
Corrections – Capital projects	Decrease	Increase	-426 capital and -388 operating over 4 years
Education – School Property	Decrease	Increase	-1 operating in 2004/05, -3 in 2005/06, -7 in 2006/07, -12 in 2007/08, and -18 in 2008/09 -55 capital in 2004/05, -125 in 2005/06, -125 in 2006/07, -125 in 2007/08 and -121 in 2008/09
Health – District Health Board deficits	Decrease	Increase	-100 in 2004/05, unquantified in outyears
Health – Orthopaedics	Decrease	Increase	-18 operating in 2005/06, -25 in 2006/07, and -30 in 2007/08
Immigration – Immigration Policy	Decrease	Increase	from -80 to -160 capital per annum
New Zealand Defence Force – Environmental Clean-up of Devonport Seabed Contamination	Decrease	Increase	-15 operating over two years
New Zealand Defence Force – Stand-alone Security Response Organisation	Decrease	Increase	-2 operating in 2005/06, -5 in 2006/07, -9 in 2007/08 and outyears -25 capital over 3 years
Revenue – Exemption for overseas earnings	Decrease	Increase	From -10 to -13 operating per annum

Risks as at 2 December 2004	Operating balance/net worth	Gross Debt	($million)
Revenue – Fringe benefit tax review	Decrease	Increase	-49 operating from 2006/07
Revenue – Tax simplification for small and medium enterprise	Decrease	Increase	-30 operating in 2006/07 and -37 in 2007/08 and outyears
Unchanged Risks			
Child, Youth and Family Services – Residential Services Strategy 2003	Decrease	Increase	-7 operating 2004/05 rising to -30 in 2008/09 and outyears -27 capital in both 2006/07 and 2007/08
New Zealand Defence Force – Defence – Capital Injections	n/a	Increase	-749 capital over 6 years
United Nations Convention on the Rights of the Child	Decrease	Increase	-20 from 2005/06

Unquantified Risks

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

Risks as at 2 December 2004	Operating balance/net worth	Gross Debt
New Risks		
Education – Student Support	Decrease	Increase
Finance – National Rail Network	n/a	Increase
Fisheries – Maori interest in marine farming	Decrease	Increase
Foreign Affairs and Trade – Official Development Assistance	Decrease	Increase
Internal Affairs – Review of Rates Rebate Scheme	Unclear	Unclear
Health – Disability Support and Aged Care Services	Decrease	Increase
Health – High and Complex Intellectual Disability Services	Decrease	Increase
New Zealand Defence Force – Overseas Deployments	Decrease	Increase
Revenue – Amortisable Research and Development Expenditure	Decrease	Increase
Savings and Home Ownership	Decrease	Increase
Social Development – Social Assistance Work Programme	Unclear	Unclear
State Services – State Sector Retirement Savings Scheme	Decrease	Increase
Transport – Toll Road Funding	n/a	Increase
Transport – Wellington Transport Package	Decrease	Increase

Risks as at 2 December 2004	Operating balance/net worth	Gross Debt
Changed Risks		
Environment – Climate Change	Unclear	Unclear
New Zealand Defence Force – Defence Capability and Resourcing Review	Decrease	Increase
Pay and Employment Equity	Decrease	Increase
Revenue – Tax and Depreciation	Unclear	Unclear
Unchanged Risks		
Agriculture and Forestry – Lower North Island Storm: On-farm Relief Measures	Decrease	Increase
Education – Tertiary Education Funding Category Review	Unclear	Unclear
Education – Wananga Capital Injection	n/a	Increase
Finance – Crown Overseas Properties	Decrease	Increase
Health – Wage bargaining	Decrease	Increase
Holidays Act 2003	Decrease	Increase
Housing – HNZC's Long-term Capital Requirements	Decrease	Increase
Housing – State Housing Project at Hobsonville	n/a	Increase
Justice – Ministry of Justice Baseline Review	Decrease	Increase
Lands and Conservation – Achievement of the Government's Objectives for the South Island High Country	Decrease	Increase
New Zealand Defence Force – Sale of Skyhawks and Aermacchi trainers	n/a	Decrease
Revenue – Taxation of Offshore Portfolio Investment/Taxation of Intermediaries	Unclear	Unclear
Revenue – Taxation of Savings and Investment Vehicles, Including Superannuation Funds	Unclear	Unclear
Social Development – Information Technology Systems	Decrease	Increase

Risks removed since the 2004 *Budget Update*

The following risks have been removed since the 2004 *Budget Update:*

Risks	Comment
Air New Zealand	Risk expired
Customs – Container Security	In forecasts
Education – Collective Employment Agreements	In forecasts
Education – Partnerships for Excellence	Does not meet criteria for disclosure
Energy – Gas Exploration	In forecasts
Health and ACC – Public Health Acute Services	In forecasts
Health – Refinancing of District Health Board Private Debt	In forecasts
Infrastructure Projects (funded by infrastructure bonds)	In forecasts
Lands – Surplus Government Property Sales	In forecasts
Maui Gas Supply	In forecasts
Relocation of NZDF Headquarters	Incorporated in NZDF – Capital Injections
Reserve Bank – Foreign Exchange Reserves	In forecasts
Revenue – Changes to the Paid Parental Leave Scheme	Does not meet criteria for disclosure
Revenue – Gaming Review	Does not meet criteria for disclosure
Revenue – Review of Tax Laws applying to the Banking Sector	In forecasts
State Owned Enterprise Capital Injections	Does not meet criteria for disclosure
Tourism – Support for Team New Zealand for 2007 America's Cup	In forecasts
Transfer of Westhaven and Hobson West Marinas to Auckland City Council	In forecasts

Statement of Fiscal Risks

Agriculture and Forestry – Lower North Island Storm: On-farm Relief Measures (unchanged, unquantified risk)

The lower North Island was hit by severe storms in February 2004 and again in August 2004. The Government approved $25 million for on-farm relief measures for the February storms. There is a risk that further funding might be necessary as the August storms not only caused further damage in the area, but also affected repairs that had already been carried out on previously affected farms. The final cost of the risk remains unquantified at this stage, but would decrease the operating balance.

Child, Youth and Family Services – Residential Services Strategy 2003 (unchanged, quantified risk)

The Department of Child Youth and Family Services (CYF) 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 $7 million in 2004/05 rising to $30 million in 2008/09 and outyears, which would decrease the operating balance. The remaining capital risk is $27 million in both 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 $426 million capital and $388 million operating funding will be required over the forecasting period for capital projects to meet future prison muster forecasts (forecast costs were $309 million capital and $153 million operating funding in the *Budget 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:

- Spring Hill Corrections Facility
- Otago Men's Corrections Facility
- Mt Eden Prison
- Auckland Women's Corrections Facility
- Expansion of the existing estate.

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

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

The Government has approved in principle 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. Financial implications will be considered as proposals are investigated and developed over a six year work programme. Individual elements of the Programme of Action will therefore be considered in future Budgets. The Programme as a whole (if fully implemented) would have total ongoing operating costs in the order of $10 million in 2005/06 rising to $50 million in 2009/10. This would decrease the operating balance.

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

Source: Ministry for Culture and Heritage.

Education – School Property (changed, quantified risk)

The Government has provided capital of $66 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. Additional capital injections could be up to $55 million in 2004/05, $125 million in 2005/06, $125 million in 2006/07, $125 million in 2007/08, and $121 million in 2008/09, with a corresponding increase in gross debt.

In addition to capital injections, consequential operating costs of $1 million in 2004/05, $3 million in 2005/06, $7 million in 2006/07, $12 million in 2007/08, and $18 million in 2008/09 are likely to be incurred, which would decrease the operating balance.

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

Source: Ministry of Education

Education – Student Support (new, unquantified risk)

The Government is considering a range of initiatives relating to Student Support. Depending on the initiatives selected. This would decrease the operating balance.

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

Source: Ministry of Education

Education – Wananga Capital Injection (unchanged, unquantified risk)

Ministers are currently negotiating with one Wananga (Maori tertiary 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, and be provided funding to bring their facilities up to a standard comparable with other tertiary institutions and to meet additional capital requirements.

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

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

Education – Tertiary Education Funding Category Review (unchanged, unquantified risk)

The Government is considering the findings of the Funding Category Review to address anomalies in student component funding rates. 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 is unclear as it depends on the options chosen.

Environment – Climate Change (changed, unquantified risk)

The Government's climate change response strategy includes a range of measures that are designed to reduce New Zealand's greenhouse gas emissions. New Zealand is a signatory to the Kyoto Protocol which imposes legally binding emission reduction targets on New Zealand. The Protocol will enter into force in February 2005, as a result of the recent decision by Russia to ratify the protocol.

The Government has announced that part of its climate change response strategy will include an emissions charge to be introduced no earlier than 2007, and capped at $25 per tonne of carbon-dioxide. Negotiated greenhouse agreements are available for some liable firms deemed to be "competitiveness at risk" by the introduction of this charge. The proposed charge would include revenue recycling to return revenue from the charge to taxpayers. However, the net impact of the charge on the operating balance is at present unclear.

An accompanying risk is that of New Zealand's net emissions position at the end of the Kyoto First Commitment Period (2008-2012). Should a net deficit eventuate, this would pose a fiscal liability to the Crown.

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 would decrease the operating balance, while capital funding would increase gross debt. Alternatively, the sale of any properties would decrease gross debt.

Finance – National Rail Network (new, unquantified risk)

The Government is considering the debt and equity needs of New Zealand Rail Corporation. Any additional equity would increase debt.

Fisheries – Maori interest in marine farming (new, unquantified risk)

Under the Aquaculture Reform Bill, the Government intends to address Mâori interests in commercial marine farming space by providing iwi with marine farming space. This is to be met through the provision of additional new space where possible, or Crown purchase of existing farms from 2008, or provision of financial equivalent of space from 2013.

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 commercial marine farm owners.

To the extent that financial compensation or Crown purchase of existing farms is necessary to address Mâori interests, this would decrease the operating balance.

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

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

Health – Disability Support and Aged Care Services (new, unquantified risk)

Volume and price increases have created cost pressures in providing disability support and aged care services. If this cost is not met within Distrcit Health Boards' (DHB) funding paths or the three-year health funding allocation it would decrease the operating balance and increase gross debt (via DHB deficits).

This risk is unquantified, as disclosure could compromise the Crown in negotiations with disability support service providers.

Health – District Health Board deficits (changed, quantified risk)

District Annual Plans submitted by District Health Boards (DHBs) indicate a combined deficit for 2004/05 in the order of $100 million with significant deficits continuing through outyears.

The Government has not agreed District Annual Plans with four DHBs. These DHBs are currently forecasting a combined deficit in excess of $90 million in 2004/05. The Government is actively discussing actions and cost-containment measures with these DHBs.

The impact on the operating balance, if any, is unclear. Any deficits that are unable to be funded from the health funding allocation will decrease the operating balance and increase gross debt (via deficits).

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

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

Source: District Health Boards

Health – High and Complex Intellectual Disability Services (new, unquantified risk)

The Government is considering the options for dealing with higher than anticipated costs associated with the provisions of the Intellectual Disability (Compulsory Care and Rehabilitation) Act 2003 and providing services to the civilian population with high and complex intellectual disability needs. Any costs above that able to be funded from the health funding allocation would decrease the operating balance.

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

Health – Orthopaedics (unchanged, quantified risk)

In 2004, the Government announced a policy of funding increased Orthopaedics operations. Completing the funding arrangement for the policy could impact on the operating balance by up to: $18 million in 2005/06, $25 million in 2006/07 and $30 million in 2007/08.

Source: Ministry of Health

Health – Wage bargaining (unchanged, unquantified risk)

Current and upcoming bargaining rounds in the health sector could result in significant increases in wage costs. If this cost is not met within District Health Boards' funding paths or the three-year Health Funding Package it would decrease the operating balance and increase gross debt (via DHB deficits).

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

Holidays Act 2003 (unchanged, unquantified risk)

The Holidays Act 2003 makes a number of changes that will have fiscal implications for the public sector. This includes any fiscal impacts relating to the fourth week of annual leave. 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 (unchanged, unquantified risk)

The Government is currently considering HNZC's long-term capital requirements in light of the demand for social housing and the need to reconfigure and modernise their housing stock. The Government will consider a number of options in 2005.

The risk is unquantified as the nature of demand for social housing has yet to be fully understood and appropriate responses have not yet been finalised. However any new capital contributions 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 Housing New Zealand Corporation (HNZC) will acquire, under the Housing Act 1955, NZ Defence Force (NZDF) land at Hobsonville deemed surplus to defence requirements but suitable for state housing purposes. NZDF land made available for purchase was acquired by HNZC at the end of 2002/03. Additional surplus land is expected to become available over the next three to four years.

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

Immigration – Immigration Policy (changed, 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. The increase in gross debt is currently estimated to be between $80 – $160 million per year, based on a flow of 40 to 80 people

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

Source: Department of Labour

Internal Affairs – Review of Rates Rebate Scheme (new, unquantified risk)

The Government is reviewing the thresholds for the rates rebate scheme. These include, for example, the maximum level of rebate paid and the income threshold for eligibility for the scheme. It is expected that a decision on this review will be taken in the context of Budget 2005. The impact, if any, on the operating balance is unclear as it depends on the option chosen.

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

The Government is reviewing the Ministry of Justice's funding requirements in order to identify sustainable funding levels and service delivery in the medium term. A report-back is expected in December 2004. 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.

Justice – New Supreme Court – Cost Escalation (new, 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 additional capital cost could range from $9 to $25 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

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 2005.

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

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

The Government is undertaking a Defence Capability and Resourcing Review to assess the medium to longer term operating needs of the NZDF. The operating pressures arise from the series of acquisitions needed to implement the Government's decisions on the future structure of the New Zealand Defence Force (NZDF) (see Capital Injection risk). These acquisitions require careful consideration of operating funding 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. In addition operating funding pressures are possible with changing operational tempo and the introduction of new capabilities. Any additional funding would decrease the operating balance.

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

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

Implementing the Government's decisions on the future structure of the New Zealand Defence Force (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 billion over 2001/02 to 2010/11, of which $251 million has been agreed, with the bulk likely to be required within the next three 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.

A process is underway to consider the individual projects of this risk as they occur, for example, the C-130 Life Extension and Upgrade project is currently being progressed. Any capital injections would increase gross debt.

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 $15 million over 2005/06 and 2006/07.

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

Source: New Zealand Defence Force

New Zealand Defence Force – Overseas Deployments (new, unquantified risk)

The Government is considering options to support overseas deployments.

This risk would, if it eventuates, decrease the operating balance.

The risk is unquantified as disclosure might prejudice the security or defence of New Zealand or the international relations of the Government.

New Zealand Defence Force – Project Protector (new, quantified risk)

The Government confirmed the acquisition of seven new patrol and sealift vessels under 'Project Protector' in 2004. The additional operating funding needs for these vessels was not fully determined at the time of the confirmation of the purchase.

Estimates are for up to $5 million in 2005/06, potentially rising up to $68 million in 2008/09 and outyears, 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 – Sale of Skyhawks and Aermacchi trainers (unchanged, unquantified risk)

As a result of the Government's decisions on the future structure of the NZDF, the NZDF is in the process of selling the Skyhawks and Aermacchi trainers. Proceeds from the sale would decrease gross debt.

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

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 $2 million in 2005/06, $5 million in 2006/07 and $9 million in 2007/08 and outyears, which would decrease the operating balance, and capital costs of $25 million from 2005/06 to 2007/08, which would increase gross debt. These costs are higher than anticipated in the *Budget Update*.

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

Source: New Zealand Defence Force

Pay and Employment Equity (changed, unquantified risk)

The Government is developing policy proposals 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 specific details of the proposals, it is not possible to estimate the fiscal costs. However, any increased operating funding would decrease the operating balance.

The risk has changed since the *Budget Update* to reflect the fact that the Government is developing proposals.

Research, Science and Technology – Health Research Package (new, quantified risk)

The Government is currently considering a health research package, which includes implementation of full-cost health research funding. The package (if fully implemented) would have total operating costs of approximately $22 million in 2005/06 rising to $39 million in 2007/08 and outyears. This would decrease the operating balance.

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

Source: Ministry of Research, Science and Technology.

Revenue – Amortisable Research and Development Expenditure (new, unquantified risk)

Due to the long lead-in period of technology companies, new investment can result in the shareholder continuity rules for carrying forward tax losses being breached. The Government is considering addressing this issue by allowing research and development expenditure to be capitalised and amortised over a future period. The effect of this proposal is unquantified but would reduce the operating balance because it would result in fewer tax losses being forfeited following shareholding changes.

Revenue – Exemption for overseas earnings (changed, quantified risk)

The Government is considering options to reduce the tax-related costs for businesses of recruiting overseas workers. Any proposal is not expected to be implemented before 2005/06.

The reduction in the operating balance could be in the order of between $10 million and $13 million per annum, depending on the options chosen.

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

Source: Inland Revenue

Revenue – Fringe benefit tax review (changed, quantified risk)

The Government is considering amendments to the fringe benefit tax regime focussing on reducing the difficulty and cost to employers of complying with fringe benefit tax. It is expected that legislative changes will become effective in 2006.

The reduction in the operating balance would depend on which proposals are finally approved and the details of the legislation. Assuming the proposals in relation to carparks do not proceed (i.e. the current treatment is maintained), the estimated net fiscal cost is approximately $49 million per annum from 2006/07.

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

Source: Inland Revenue

Revenue – Tax and Depreciation (changed, unquantified risk)

The Government is considering further issues related to depreciation, including the overall structure of depreciation and potential changes to the tax treatment of rental housing. However, the impact on the operating balance remains unclear as it depends on options chosen.

Revenue – Tax simplification for small and medium enterprise (changed, quantified risk)

The Government is progressing a number of proposals to reduce tax compliance costs for small to medium-sized enterprises. These include aligning the payment dates for both provisional tax and GST, and providing the option to pay provisional tax on the basis of GST turnover. The expected fiscal cost of these particular proposals is approximately $30 million in the first year, with an expected ongoing cost of $37 million per annum. This would decrease the operating balance.

It is expected that legislative amendments will be enacted in 2006.

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 (unchanged, unquantified risk)

Work on taxation of domestic intermediaries (which invest onshore and offshore) has commenced. This will include consideration of the taxation of both onshore and offshore investment in equity by New Zealand residents. A target date of April 2007 has been set for the implementation of these changes. The impact on the operating balance is unclear, as it will vary according to the options chosen.

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 according to the options chosen and the method of implementation.

Savings and Home Ownership (new, unquantified risk)

The Government is considering a range of issues relating to savings and home ownership levels in New Zealand, including the report of the Savings Product Working Group, and expects to consider a number of options in the context of Budget 2005. The impact, if any, of this proposal on the operating balance and debt would vary depending on the options chosen and the implementation of those options.

Social Development – Early Intervention (new, quantified risk)

Ministers are currently considering proposals for a range of social services which are designed to improve safety and security for children and young people, and to enhance their ability to fulfil their potential.

Depending on the nature and size of proposals selected, it is estimated that costs could be up to $28 million per annum operating in 2005/06, and up to $57 million in 2006/07 and outyears, with a corresponding decrease in the operating balance.

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

Source: Ministry of Social Development

Social Development – Social Assistance Work Programme (new, unquantified risk)

As follow up on Working for Families, the Government is considering options for simplifying the benefit system and reforming labour market assistance and service delivery to better support beneficiaries' entry into employment. 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). 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 attempting 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 – State Sector Retirement Savings Scheme (new, unquantified risk)

The Government is considering options for extending the employer subsidy for members of the State Sector Retirement Savings Scheme beyond 3%, 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.

Transport – Toll Road Funding (new, unquantified risk)

The Government is considering the case to proceed with a toll road, Albany-Puhoi Urban Rapid Transit (ALPURT B2), proposal by Transit New Zealand. A report is due in March 2005 providing further information on the proposal.

Transport – Wellington Transport Package (new, unquantified risk)

In May this year the Government was approached by Greater Wellington Regional Council to identify where Central and Local Government, in partnership, can make significant and timely improvements to Wellington's transport outcomes. The Government is now considering the Wellington Transport Project Group's recommendations and the relative split between Local Government and Central Government contributions to Wellington regional transport outcomes. A decision is expected early 2005. Costs would vary depending on the options chosen and may either increase gross debt and/or decrease the operating balance.

In addition, the Government may consider additional funding following the Western Corridor Transportation Study report in 2005. Potential costs are unclear at this stage.

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 year. The review is due to report back in early 2005.

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 October 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/defu/2004/.

Quantifiable Contingent Liabilities

Guarantees and indemnities	**Status[6]**	**($ million)**
Cook Islands – Asian Development Bank loans	Unchanged	18
Indemnification of receivers and managers – Terralink Limited	Unchanged	10
Ministry of Justice – Treaty settlement, tax liabilities	Changed	75
Mighty River Power Limited – guaranteed payment obligations	Unchanged	30
Solid Energy New Zealand Limited	Unchanged	42
Ministry of Transport – funding guarantee	Unchanged	10
New Zealand Railways Corporation	New	10
Post Office Bank – guaranteed deposits	Unchanged	12
Guarantees and indemnities of SOEs and Crown entities	Changed	3
Other guarantees and indemnities	Changed	17
		227
Uncalled capital		
Asian Development Bank	Changed	1,086
European Bank for Reconstruction and Development	Unchanged	13
International Bank for Reconstruction and Development	Changed	1,204
		2,303
Legal proceedings and disputes		
Air New Zealand Limited – legal claim	Unchanged	107
Health – legal claims	Unchanged	104
Tax in dispute	Changed	471
Transpower New Zealand Limited	Unchanged	20
Other legal claims against SOEs and Crown entities	Changed	7
Other legal claims	Changed	89
		798
Other quantifiable contingent liabilities		
International finance organisations	Changed	1,210
Reserve Bank – demonetised currency	Unchanged	23
Social Development – claim for judicial review	Changed	48
Other quantifiable contingent liabilities of SOEs and Crown entities	Changed	70
Other quantifiable contingent liabilities	Changed	32
		1,383
Total quantifiable contingent liabilities		**4,711**

6 Relative to reporting in the 30 June 2004 *Crown Financial Statements*.

Unquantifiable Contingent Liabilities

Institutional guarantees	**Status**
Accident Compensation Corporation (ACC) litigations	Unchanged
Asure New Zealand Limited	Unchanged
At Work Insurance Limited	Unchanged
Auckland rail lease	Unchanged
Bona Vacantia property	Unchanged
Building Industry Authority litigation	Unchanged
Crown research institutes	Unchanged
Ministry of Defence – litigation	Unchanged
District Court Judges, Justices of the Peace, Coroners and Disputes Tribunal	Unchanged
District health boards – director indemnity – (DHBs)	Unchanged
District health boards (DHBs) – Auckland DHB	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	New
Housing New Zealand Corporation	Unchanged
Indemnities against acts of war and terrorism	Unchanged
Kyoto Protocol	Changed
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 Ltd – purchase of rail network assets	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	Unchanged
New Zealand Post Primary Teachers' Association	Unchanged
Sale of Crown assets	Unchanged
Treaty of Waitangi claims	Unchanged
Treaty of Waitangi claims – settlement relativity payments	Unchanged