

# ANNUAL REPORT

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for the year ended 30 June 2005



# WHAT WE DO

## The Treasury

At the Treasury our job is to help the Government to improve economic performance and manage scarce resources. All of this is focused on improving living standards for New Zealanders.

The Treasury has four main roles:

- We provide advice to improve the economic and fiscal conditions for high levels of economic growth and improved living standards.
- We monitor and manage the financial affairs of the Crown.
- We assess and test other agencies' advice and proposals which have economic and financial implications.
- We provide leadership, with other central agencies, to develop a high-performing State sector.

The Treasury provides advice and services through nine output classes provided to the Minister of Finance through Vote Finance.

## Crown Company Monitoring Advisory Unit (CCMAU)

CCMAU is responsible for maintaining and enhancing the Crown's ownership interest in Crown research institutes (CRIs), State-owned enterprises (SOEs) and a number of Crown-owned companies and entities. CCMAU provides advice to relevant Vote Ministers through output classes under Vote Crown Research Institutes and Vote State-Owned Enterprises.

## The Treasury/CCMAU relationship

CCMAU is a stand-alone unit within the Treasury. The Executive Director of the Unit is directly accountable to the Secretary to the Treasury for the Crown's investment in CCMAU, and for CCMAU's performance.

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## MINISTER'S FOREWORD



The Treasury, as the Government's lead economic and financial advisor, has a significant role in helping achieve our goal of growing an inclusive economy for all New Zealanders.

This *Annual Report* outlines the contribution the Treasury has made over the 2004/05 year to support this central aim.

A particular focus has been ongoing work by the Treasury to lift New Zealand's economic growth and productivity and to maintain the Government's role as a careful fiscal manager, supported by a high-performing State sector.

The Government has also received valued Treasury support through its running of an effective 2005 Budget process and through advice and analysis on a range of issues as set out in this report. In particular, I have welcomed their work on the savings package announced in the Budget and their contribution towards addressing productivity and trans-Tasman harmonisation issues.

As Minister of Finance I know I can look to the Treasury for high-quality analysis and policy advice in progressing Government goals and raising living standards for New Zealanders.

A handwritten signature in black ink, appearing to read 'M. Cullen', followed by a long horizontal line extending to the right.

Hon Dr Michael Cullen  
Minister of Finance

## HIGHLIGHTS OF OUR YEAR

- Reporting on economic performance and identifying critical issues for growth, particularly to improve workplace productivity.
- In collaboration with the Ministry of Economic Development (MED), further developing the Growth and Innovation Framework and publishing *Economic Development Indicators 2005*.
- Reporting on the Review of Major Financial Institutions with agreement to establish a Joint Trans-Tasman Council on Banking Supervision.
- Providing advice on the Budget savings package *Securing Your Future*.
- Supporting the Public Finance (State Sector Management) Bill through the House and implementing legislative changes to improve State sector performance.
- Working with other officials to monitor implementation of the Working for Families package.
- Providing advice on demographic and fiscal issues affecting health and education.
- Providing advice on transport and infrastructural issues.
- Completing long-term hold reviews of four SOEs, with three further reviews in progress (Treasury and CCMAU).
- Implementing organisation-wide outcome plans and management objectives.
- *2004 Treasury Climate Survey* confirming overall staff satisfaction and progress on cultural change.

## CHIEF EXECUTIVE'S SUMMARY



I am pleased to present this *Annual Report for the Treasury for the 2004/05 year*.

Over the past 12 months, the Treasury has continued to concentrate on its primary role of providing quality economic and financial policy advice for the Government. Our efforts have been clearly focused on achieving the Government's long-term goals, as well as providing an effective contribution to more immediate issues as they arise.

One particularly positive feature of the year has been the opportunity to take a step back from our day-to-day work to address a number of "big picture" issues for the Government. These have included the development and implementation of a workplace savings scheme, finding new ways to increase New Zealand's workforce productivity and progress towards a single economic market with Australia.

We are also involved in several projects to consider long-term performance and productivity issues in important areas such as tertiary education, health and innovation.

The Treasury has made good progress towards refining and implementing our new strategic direction. We have developed detailed "game plans" for our five outcome areas, incorporating both new and business-as-usual work. Staff across the Treasury have delivered a large number of high-quality outputs that, in total, have helped us make some real headway towards our key outcomes.

### Investing in our people

"Investing in our people" is one of the Treasury's four management priorities, and I am pleased to report a range of significant achievements that have all contributed towards making the Treasury a better place to work.

Our accommodation changes are now complete, resulting in positive feedback from across the organisation. In the latest Treasury climate survey, the Treasury's overall score amongst staff continued to trend upwards, with particular improvements in how staff view career opportunities, teamwork and knowledge sharing. Our people continue to be significantly more positive than their peers in other New Zealand organisations.

The capability of our staff – including senior staff – has been another area of focus. The recommendations of a group set up to review senior staff capability

have now been implemented, involving clarifying and refocusing senior roles, and creating a more flexible work reallocation process.

In addition, a project reviewing wider capability issues reported in April, with resulting initiatives going forward into 2005/06. The project report identified some technical, managerial and relationship management skill gaps, and provided recommendations on learning and development strategies to address these.

## Engaging effectively

Over the past year we have taken a more structured approach to our engagement with external stakeholders, with a particular focus on interaction with business and local government communities. The input we receive from meeting and working with our external stakeholders is invaluable in helping us to set and refine our priorities going forward.

The Treasury also participated in the Hui Taumata Māori economic development conference held in Wellington in March. The Treasury provided a discussion paper and other material for the conference, which contributed to very positive and useful dialogue with an important sector of the community.

Our people regularly work together with their colleagues in other Government organisations. A recent example of this collaboration was the publication of *Economic Development Indicators 2005*, a joint project between the Ministry of Economic Development and the Treasury. Economic indicators allow us to monitor progress towards economic goals and to benchmark New Zealand's performance against that of other countries in the OECD. *Economic Development Indicators 2005* measures a wide range of productivity and growth determinants such as material standards of living, labour utilisation, productivity, investment and innovation. These indicators are intended to complement the Government's broader set of sustainable development and social indicators, as well as creating a basis for public discussion on ways to improve New Zealand's economic performance.

## Crown Company Monitoring Advisory Unit (CCMAU)

CCMAU is a stand-alone unit within the Treasury that monitors Crown research institutes, State-owned enterprises and Crown-owned companies and entities – organisations which together play a significant part in New Zealand's economy.

Developing and refining the unit's new strategic direction has been a major priority for CCMAU over 2004/05. An important objective of this work has been to engender a sense of pride and identity amongst the CCMAU team. The latest Treasury climate survey reflects the success of these efforts, with a 10% increase in CCMAU's overall score.

## The year ahead

We enter the 2005/06 year with the aim of making further progress towards our vision of becoming a world-class Treasury working for higher living standards for New Zealanders.

Being a world-class Treasury means many things. It requires us to be outcome driven, to deliver results in the areas that matter most, to accurately anticipate issues and, perhaps most importantly, to employ talented people with the right support systems in place that enable them to use their skills most effectively. I am confident that the progress we have made over the past year has taken us another significant step towards achieving this vision, and I would like to thank all Treasury staff for their contribution in helping to make this happen.

A handwritten signature in black ink that reads "John Whitehead". The signature is written in a cursive style with a large initial 'J'.

John Whitehead  
Secretary to the Treasury

### Bringing a global perspective to our work

Being a world-class Treasury is part of our vision, but judging how well we are fulfilling this vision is not a straightforward task. Assessing how we perform relative to our peers – other Treasury or Ministry of Finance organisations around the world – is difficult because of the slightly different functions each organisation performs. It can be like comparing apples and oranges.

There are, however, management issues and other challenges that we have in common with many of our overseas counterparts and where we can learn from each other. During 2004/05, we exchanged information with Her Majesty's Treasury in the United Kingdom as well as Australian federal and state Treasuries.

In February 2005 the Treasury took part in the inaugural meeting of the Australia-New Zealand Treasuries Corporate Managers Network. The meeting proved to be an excellent forum for discussing shared areas of core business and corporate issues, including Knowledge Management, recruitment, staff development, information technology, service level agreements and contract management. The value of the event for the Treasury and other participants has led to plans for another Network meeting before the end of the year.

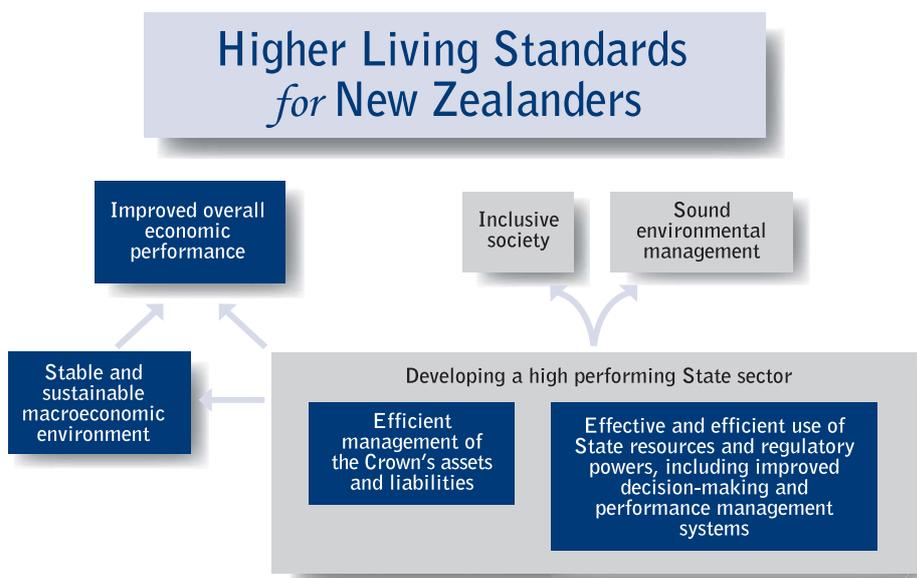
Looking ahead, we are committed to furthering the exchange of information and best practice with our international peers to ensure we remain a world-class Treasury.

## OUR OUTCOME CONTRIBUTION

The Government has a goal of growing an inclusive economy for the benefit of all. Reaching this goal requires higher living standards for New Zealanders. This is the overarching vision for the Treasury.

A series of outcomes supports this vision – the areas where we are well placed to make a positive contribution to the Government’s goals. These are key outcomes for the Minister of Finance, or for Vote Ministers in the case of CCMAU.

The Treasury’s outcomes are articulated individually (refer to the blue boxes in the diagram below), and we use them as goals to focus our efforts. We also have a role in making sure they all work together, and in considering how best as a whole our work underpins our overall vision for New Zealanders.



As the Government’s primary economic and fiscal advisors, we bring a particular perspective to achieving these outcomes. We also work alongside other agencies to achieve the desired results.

In some cases – such as an inclusive society and sound environmental management – other agencies take the lead, but we are centrally involved, as these areas are important to us.

As a central agency, we continue to work with the State Services Commission (SSC) and the Department of the Prime Minister and Cabinet (DPMC) towards

developing a high-performing, trusted and accessible State sector – which delivers the right things in the right way, at the right prices. We each bring our different perspectives to this outcome, and in turn it contributes to other outcomes.

During 2004/05 we refined our desired outcome contribution, drawing in our business-as-usual work. As a result, this document reports against the direction set out in our *Statement of Intent* (SOI) for 2004/05.

In this section we report on progress during 2004/05 and the challenges ahead, in the context of improved outcomes for the Government in the longer term.

## Improved overall economic performance

### Overview

The Government continues to place a high priority on policies designed to promote economic growth and to improve living standards (Prime Minister's 1 February 2005 *Statement to Parliament*). As the Government's chief economic advisor, our role is to understand what drives growth in New Zealand's average income and advise the Government on the impact a wide range of policies will have on growth.

In *Growing an Innovative New Zealand 2002*, the Government set out its economic objective to return New Zealand to the top half of the OECD in terms of real GDP per capita and maintain that standing. New Zealand's current ranking is 20th out of the 30 OECD countries. An increase in growth since the early 1990s has arrested the earlier decline in GDP per capita relative to the OECD. Growth in GDP per capita increased to the point where it averaged 2.3% between 1993 and 2005. New Zealand needs to sustain this growth in order to increase its OECD ranking.

Growth in GDP per capita since the early 1990s came initially from growth in labour utilisation and more recently from labour productivity growth, which by the late 1990s had become the dominant source of growth in GDP per capita. It is expected to remain so over the next five years as indicated in Table 1.

Table 1 – New Zealand economic growth rates: history and forecasts

	March years**	
	1993 to 2005	2006 to 2009
GDP per capita growth* %	2.3	1.9
GDP growth* %	3.5	2.8
Labour productivity growth %	1.1	1.7
Labour utilisation growth %	1.2	0.2
Population growth %	1.2	0.9

Notes:

\* GDP per capita growth is the sum of the growth rates for labour productivity and labour utilisation (or GDP growth less population growth). GDP growth is the sum of the growth rates for labour productivity, labour utilisation and population.

\*\* Average of the March year annual average percent changes derived from the Treasury's 2005 Pre-election Economic and Fiscal Update.

The Treasury's role is to understand what determines growth in New Zealand per capita income and advise the Government on how the wide range of policies it considers (including institutions, regulations, ownership, expenditure and revenue options) will affect economic growth.

#### Our desired outcome contribution

- Reporting annually on progress and critical issues for growth to help with setting strategic priorities.
- Developing a sound understanding of New Zealand firm productivity growth and the factors that influence firm productivity, including the role of taxation, product market regulation, firm finance and innovation.
- Removing barriers to labour force participation, including improving education attainment, skills and labour mobility.
- Improving regulations and institutions – particularly those related to property rights and resource management, infrastructure and external linkages.

#### Our progress

Improving economic performance has been our focus for a number of years. Further analysis identifies the above priorities for the Treasury and they provide a basis for an agreed Treasury-wide plan to prioritise and implement growth policy work. Identifying and discussing with the Minister of Finance the critical issues for New Zealand growth is an important part of the prioritisation process. The growth programme involves collaborative work with other agencies, and we have developed a communication strategy to keep internal and relevant external parties informed of the status of the various growth projects and to raise important issues.

We have taken up opportunities to share our current thinking on economic growth and have encouraged and participated in intellectual debate:

- At the request of the Hui Taumata Steering Committee, we produced a background paper on Māori economic development for Hui participants, and the Secretary to the Treasury participated in a panel session. This work stimulated debate and discussion on the key drivers of Māori economic development, including consideration of the important role that institutions play in mediating the way in which people, enterprises and assets contribute to economic development.
- We collaborated with MED to complete the Growth and Innovation Framework *Economic Development Indicators Report* for publication in February 2005. We have been involved in MED-led reports on further developing the indicators. The February report created a basis for discussion in the public arena on ways of lifting New Zealand's economic performance through innovation.

- We assisted a visit by OECD officials during their preparation of the 2005 OECD Economic Survey of New Zealand. The Survey report provided a comprehensive review of New Zealand's economic performance and policies. The analysis and accompanying recommendations provide many opportunities for further discussion and debate among policy-makers.

We have continued to accumulate knowledge on what matters for growth and have applied this when delivering policy advice to the Minister of Finance. We reported to Ministers on Government support for business research and development and worked with MED and the Ministry of Research, Science and Technology (MoRST) on support for private sector research and development. The Treasury is undertaking a review of the contribution of technology to growth and a review of the innovation system.

We continued to work with other departments, particularly the Ministry for the Environment, MED and the Department of Conservation, to provide advice on ways to improve the functioning of the Resource Management Act. We played an advisory role in the direction taken by the Water Programme of Action. We also largely completed a project on road transport funding that focuses on the methodology for selecting specific projects and this work will inform our briefing for the incoming government.

The impact of taxation on growth is an area that is being given more attention. In the 2004/05 year we provided advice on potential growth-enhancing policy options to encourage business development. We also provided advice on changes to the Overseas Investment Act and supported the Finance and Expenditure Committee's examination of the legislation, providing clarity on conditions for overseas investment and higher thresholds for investment.

We commenced work on a project on climate change mitigation and the impact on economic growth. This work will include an analysis of the growth implications from the Kyoto agreement.

We have several ongoing projects on international trade and other international linkages. Advice was provided on the closer economic relations work with Australia in August 2004. We are now leading development work on the Single Economic Market that Ministers Dr Cullen and Mr Costello agreed at their bilateral meeting in February. We continue to participate in Free Trade Agreement talks as part of the New Zealand team.

Extending our understanding of the key drivers of growth was an important component of our work over 2004/05. This has enabled us to apply a growth-lens to policy questions.

We have worked with other agencies to understand New Zealand's labour force participation and the potential contributions to growth. In April 2005, a workshop on labour force participation and economic growth was jointly hosted by the Treasury, the Ministry of Social Development (MSD), the Ministry of Women's Affairs and the Department of Labour. This brought together local knowledge and the best understanding and evidence on economic growth and participation from around the world.

We undertook research on the way the labour market is adjusting to current and predicted skill and labour shortages and contributed to interdepartmental advice on various initiatives to address these shortages. We also contributed to cross-departmental advice on options to increase the participation choices of parents and improve the incentives faced by secondary earners. This included contributions to the design of the single core benefit framework, focusing on how the framework could be used to raise labour force participation.

Our outcome plan emphasises the importance of understanding labour productivity growth. We co-hosted a productivity workshop in July 2004 with the Reserve Bank and MED. We continued to contribute to the Workplace Productivity Working Group, including a study of the links between literacy and economic growth.

Understanding what matters for growth at the firm level will enhance our understanding of the influences of the business environment on firm productivity growth. Projects comparing the characteristics and turnover of New Zealand firms with other OECD countries and how firm turnover and growth contribute to labour productivity growth were completed.

Work has also focused on understanding the role of capital accumulation and its links to productivity growth. This work has evaluated the reason for New Zealand's relatively low rate of capital accumulation and the factors influencing the accumulation. It has also included consideration of the influence of financial markets and financial systems, and of other institutions that have an influence on firm investment and innovation.

### Workforce participation programme

Who is and is not participating in the workforce is of significant interest to the Treasury, as part of its drive to improve economic growth.

Increased labour productivity is a key to economic growth, and workforce participation is one of several factors contributing to labour productivity.

Although New Zealand's current rate of workforce participation is high compared with other OECD countries, it remains lower than average amongst particular groups.

While the decision to participate in the workforce is essentially a personal one, there are many things the Government can do to affect that decision, particularly in areas such as labour market policies, the tax system, the welfare system and child care.

The Treasury's workforce participation programme has three key objectives: to increase our understanding of New Zealand's workforce participation rate, to evaluate prospects for improvement and what role the Government might play, and to understand which policy options are most likely to encourage higher workforce participation.

An important component of this work involves collaborating with other government agencies such as MSD, the Department of Labour and Ministry of Women's Affairs to develop a suite of options that will encourage different choices around workforce participation.

The work is being driven by a cross-agency steering group, led by the Department of Labour, with individual members having overall responsibility for each workstream. Specific groups of people are considering workforce participation drivers such as early childhood education and out-of-school care, labour market transition issues, workplace culture and practices, and income barriers. The Treasury is leading a number of these workstreams.

The result of this work will be a clear set of policy options, and the implications of each, for consideration by the Government.

Feeding into this process was a workforce participation workshop held in April this year. Jointly sponsored by the Treasury, MSD, the Ministry of Women's Affairs and the Department of Labour, the workshop brought together local knowledge and research, coupled with the best understanding and evidence on economic growth and participation from around the world. Participants included Government officials, academics and non-governmental organisations.



Nathan McLellan and David Law worked on labour productivity

### Challenges ahead

New Zealand needs to sustain a relatively high growth rate in order to continue to lift its income relative to the OECD. This will be a challenge. The Treasury's most recent forecasts reflect an expected cyclical slowdown in the near term and incorporate the view that over the next five years growth will be sustained rather than accelerate.

A major factor contributing to the strong growth since the early 1990s has been growth in labour utilisation. However, now that New Zealand's level of labour utilisation is among the highest in the OECD, it is not surprising that many industries are running into increased costs in obtaining labour and skills required. Other factors that are expected to impinge on growth are the capacity to meet the rising demand for transport and energy, the demands for better resource allocation including water quality, and obligations under the Kyoto Protocol.

The greatest scope for increasing New Zealand's growth rate, at least over the longer term, lies in raising labour productivity growth. Relatively low levels of

multifactor productivity and low capital investment growth of the past have meant that New Zealand's level of labour productivity is still very low relative to most other OECD countries. Although there was an increase in labour productivity growth after the mid-1990s, current projections still imply a growth rate of labour productivity below the historical OECD average of about 2% per year.

The focus of our growth outcome work for 2005/06 will be:

- an overview role in monitoring New Zealand's growth performance, and identifying and reporting on critical growth policy issues
- specific projects aimed at identifying areas where there is potential to enhance conditions that impact on firm productivity, investment and employment growth.

This includes developing a sound understanding of New Zealand firm productivity growth and of the factors that influence firm productivity. This work will have an emphasis on identifying policy contributions to raising labour productivity growth, recognising that such contributions can come from several sources including from the characteristics of labour, product and financial markets, and the education system for instance.

In the longer term, as productivity growth increases, the emphasis of the work may change but the importance of sustained higher labour productivity growth will be enduring.

#### Feedback on economic performance

"...increases in real GDP per person have outpaced the OECD 10-year moving average since 2000, putting the country on track towards achieving the Government's longer-term objective of lifting GDP per person back into the top half of the OECD... This is a deserved reward for the wide-reaching macroeconomic and structural reforms put in place over the past 20 years."

Source: OECD Policy Brief for Economic Survey of New Zealand 2005 ([www.oecd.org/publications/Pol\\_brief](http://www.oecd.org/publications/Pol_brief))

## Stable and sustainable macroeconomic environment

### Overview

A stable and sustainable macroeconomic environment is an essential precondition for achieving the Government's objective of growing per capita income. It allows individuals, businesses and the Government to plan more effectively for the longer term, thus improving the quality and quantity of investment in physical and human capital, and helps to raise productivity.

A stable and sustainable macroeconomic environment requires good fiscal management, good monetary policy and financial stability, as well as reliable information on fiscal and economic variables. Our role is to provide advice on macroeconomic and fiscal policy. We also provide timely and accurate economic and fiscal data, firstly through economic and fiscal forecasts and secondly through reporting through the Crown accounts. In fulfilling these roles we work closely with the Reserve Bank, MED and other relevant agencies for monetary and financial stability, and all departments to ensure a sustainable fiscal position.

#### Our desired outcome contribution

- Advising on the sustainability of fiscal policy in both the short and long term.
- Monitoring the performance of the current Budget frameworks and developing options for revising them if necessary.
- Further analysing the resilience of our fiscal and monetary policy institutions/settings to domestic or international shocks, and advising on how shocks are transmitted through the economy.
- Examining and, where necessary, refreshing our economic and fiscal forecasting processes.
- Further developing our understanding of cyclical and trend developments with respect to growth and other key macroeconomic variables.
- Increasing our understanding of the complementarities and trade-offs in anchoring inflation expectations, stabilising output and moderating fluctuations in financial and asset markets.
- Monitoring and advising the Minister of Finance on the Reserve Bank's performance and working with the Reserve Bank to advise on monetary and financial policy, regulation and governance as appropriate.

#### Our progress

##### Economic performance

In the 2004/05 year, the economy continued to do well. The economy grew at 4.2% in the year to 31 March 2005, translating into real growth per capita of 2.9%. This was largely driven by continuing income growth and rising household wealth, stemming from the strong labour and housing markets, and high international commodity prices. Strong economic growth saw unemployment fall to low levels (3.7% as at June 2005) and many businesses operating at near-to-full capacity.

High economic growth has been associated with a rising inflation rate (2.8% annual CPI inflation for the June 2005 quarter). This reflects strong cost and price pressures in domestically focused parts of the economy, which have been partly offset by continuing low inflation in import prices and in those parts of the economy more exposed to international competition. As a consequence, the Reserve Bank announced a number of interest rate increases in 2004/05. Strong

domestic demand growth and the high exchange rate also saw a high current account deficit (7% of GDP in the year to March 2005).

In the 2004 *Fiscal Strategy Report* the Government announced that it was altering its fiscal objectives to reflect requirements under the Public Finance Act to specify a timeframe for its objectives and to lock in recent progress toward its objectives. In particular, it lowered the gross debt to GDP objective to a target of passing through 20% before 2015. Latest forecasts show the Government on track for achieving this objective.

The strong growth in the economy has recently shown signs of slowing, and annual growth rates are expected to ease over the next two years. This reflects the effects of some cyclical factors in the economy, such as the flow-on effect of higher interest and exchange rates, lower net migration, slower trading partner growth and an expected easing in commodity prices. Growth is then forecast to pick up in 2007/08 to reach rates of around 3% per annum (or 2% per capita) once the cyclical factors play out.

### Treasury contribution

In 2004/05 our contribution to this outcome centred around the preparation of economic and fiscal forecasts and monitoring information, as reported in the Economic and Fiscal Updates and the Government's *Budget Policy Statement* and *Fiscal Strategy Report*. We continued to support the systems and processes, and provided advice, for the preparation of the Government's 2005 Budget.

As well as the fiscal analysis required for Budget decisions, we reviewed the fiscal policy impacts on the wider macroeconomy since 1960, reviewed and recommended a change to the assumptions regarding the rate of return of the Crown Financial Institutions (CFIs) and initiated a review of the Budget process, including a diagnosis of the issues surrounding the current Budget system.

The Public Finance Amendment Act passed in late 2004 includes a number of important reforms. In the context of this outcome goal, one key change is the requirement for the Treasury to prepare a statement of the long-term fiscal position – looking out at least 40 years. The statement will seek to identify the key drivers of long-term fiscal trends and the parameters open to policy-makers that would help manage long-term demographic and other influences on the long-term fiscal position. Preparatory modelling and analysis work for the first statement – due to be released in the first half of 2006 – commenced in 2004/05.

In 2004/05, we continued our work on the implementation of the International Financial Reporting Standard accounting policies to the Crown Financial Statements. We also advised on the accounting treatment of significant policy issues that arose in the course of the year, for example the foreshore and seabed issue and the Kyoto Protocol. We continued to advise on other accounting policy issues, such as Financial Reporting Standards Board (FRSB) exposure drafts.

We contributed to the development and maintenance of New Zealand's monetary policy framework by reporting on the performance of monetary policy and the Reserve Bank's policy targets agreement, and advising on the 2005-2010 Reserve Bank funding agreement. We also contributed to the review of Major Financial Institutions, alongside the Reserve Bank and MED. This review reported to the Minister of Finance in early 2005.

The Treasury's work does not have a one-to-one impact on the key macroeconomic variables and institutions. Rather, the impact of our work was to:

- provide high-quality advice to the Minister of Finance so that he could make timely and informed fiscal policy decisions
- provide information to both the Government and private sector on actual and prospective economic and fiscal results, to help improve the basis for their decision-making
- keep the Government on track for the full implementation of the new international accounting standards from 2007. Implementing these standards will give enhanced credibility and transparency to the Government's published fiscal information
- enable the passage and implementation of the Public Finance Amendment Act 2004 – for example, the presentation of the 2005 Budget material in GST-exclusive terms. The changes made as a result of implementing the amended legislation are expected to both reduce “noise” in the system and improve public sector performance more directly through, for example, improving coordination among agencies.

### Challenges ahead

Although the core policies and institutions supporting the macroeconomic environment are considered to be sound, there will be a number of pressures ahead. Some of these relate to the rise in CPI inflation and the current account deficit, while a slowing economy and the pace of recent spendings could place some pressure on fiscal policy. Our work will continue to focus on these issues, as well as the preparation of the first published *Long Term Fiscal Report* and the full implementation of the Public Finance Amendment Act.

### Taking a close look at what's far ahead

Along with many other countries with ageing populations, the Treasury has been looking at the effects of evolving demographics on the government's long-term fiscal position for almost a decade.

As the proportion of the population over 65 grows, this has an impact on the Government's finances. More money may be needed to fund superannuation, health care and other services for the older population. But at the same time, other large spending requirements may also have an impact, such as the replacement of public transport infrastructure, defence equipment and public housing. This could add to pressure on the Government's finances. Sustaining the fiscal position will require governments to make policy trade-offs between spending categories and between public and private provision.

In future, the Treasury will be formally reporting on the long-term fiscal position to provide more information for decision-makers and the general public. These reports will cover a period of at least 40 years into the future. Changes to public finance legislation mean that reporting is now compulsory. The first report will be tabled by 30 June 2006 and at least every four years after that.

The long-term fiscal report project is being led by Paul Rodway, with help from John Janssen, Dasha Leonova and Peter Wilson.



Long-term fiscal report project team – Paul Rodway, Dasha Leonova and John Janssen (absent Peter Wilson)

## Effective and efficient use of State resources and regulatory powers, including improved decision-making and performance management systems

### Overview

The effective and efficient use of State resources and regulatory powers contributes to a wide range of the Government's desired economic, social and environmental outcomes. The Treasury is responsible for monitoring and managing the Crown's financial affairs and advising the Government on how to get the best quality and value out of public spending.

Well-designed decision-making and performance management systems (including the Budget) encourage excellent performance in departments and Crown entities and sound financial management. They also help in making decisions on trade-offs and performance monitoring over time. We are constantly working to improve State sector decision-making and performance management systems.

The Treasury has the primary responsibility for advising on the Budget process and the Public Finance Act, preparing the Crown accounts, and designing financial and reporting arrangements for SOEs and Crown entities. We also work with SSC in designing systems that encourage and maintain public sector effectiveness and accountability.

### Our progress

We have continued to provide advice to the Government on the effectiveness and efficiency of spending and regulation, and on systems and processes that support those goals.

Work which has assisted the Government with advice on the effectiveness and efficiency of spending and regulation has included:

- working with Inland Revenue, MSD and SSC in monitoring the implementation of the Working for Families package
- working with the Department of Labour on capability- and strategy-related issues arising from its repositioning exercise
- working with the Department of Labour and MSD to provide advice on the restructuring of community employment activities
- completing and reporting on the Review of Major Financial Institutions, and subsequent work on a Joint Trans-Tasman Council on Banking Supervision, regulation of non-bank financial institutions and institutional arrangements for financial regulation
- providing advice with other departments on changes to the Resource Management Act to provide for more certainty through better planning and better decision-making on resource consents
- contributing to central and local government work on infrastructure issues, such as Auckland, energy and transport
- providing advice on issues associated with climate change and Kyoto Protocol commitments.

### Monitoring the implementation of Working for Families

The Treasury, in conjunction with SSC, monitors the implementation of the Working for Families (WFF) package. During our earlier work with SSC, MSD, Inland Revenue and other agencies on policy development for WFF, it was recognised that central agencies should independently monitor the delivery of the package to ensure it achieved its objectives.

The WFF package is unusual amongst government initiatives; not only because of its broad scope but because it is jointly delivered by two agencies – Inland Revenue and MSD. A high degree of coordination between the two large agencies, whose roles and IT systems are quite different, is needed to ensure that services can be provided seamlessly and on time. The delivery of income supplements to customers on a weekly basis is also an expansion of Inland Revenue's role.

As part of our monitoring activities, the Treasury and SSC met regularly with MSD and Inland Revenue during 2004/05. In addition, the Treasury and SSC review and approve the monthly reports prepared by MSD and Inland Revenue for the Minister for Social Development and the Minister of Revenue. These reports provide information on implementation progress of the various components of WFF, including actual numbers of applicants compared with the numbers forecast, and identify any issues or associated risks and what actions are required to address them.

Work on the systems and processes that support and encourage the effective use of resources and promote high performance has included:

- development of the Public Finance (State Sector Management) Bill, assisting with its passage through the legislative process and subsequent implementation
- reviewing the 2004 Budget process and systems and implementing improvements in the 2005 process
- beginning a review of the long-term design of the Budget system so that it would provide effective support for both the Government's fiscal strategy and its desire for improved performance from the State sector
- working closely with DPMC and SSC to agree a shared outcome for central agencies around performance in the public sector. The focus is on ensuring that central agencies work effectively together to support Ministers in promoting and achieving improved performance in the public sector.

### Challenges ahead

There is growing demand for evidence on the effectiveness of Government policies – whether they have achieved their intended aims, and identifying the most effective mix of government services and regulations. This means the Treasury and other central agencies have a role in working with other agencies to target research and evaluation work, support the development of evaluation techniques and help disseminate evidence on good practice.

Managing for outcomes encourages government departments to focus on the capabilities they need, the risks they must manage and the evidence they need

to demonstrate success. Central agencies have been providing training and help with this process. The challenge remains to get value from these changes.

Another result of managing for outcomes is a greater focus by Crown entities on the outcomes to which they are working, including choosing what they produce in contributing to those outcomes. To support this, strategic priorities need to be better developed and assessed at both whole-of-government and agency levels. We believe there is potential for Budget processes to assist more with this goal.

Effective design and delivery of government policy depends increasingly on coordination among government agencies. As a central agency, the Treasury has a role in responding to the resulting demand for “joined-up government”. This role has seen us increasingly become involved in identifying issues that span several agency boundaries; encouraging agencies to coordinate and provide seamless delivery for the public; and reviewing the extent of coordination. We also have an ongoing responsibility to ensure our own advice supports these objectives.

## Efficient management of the Crown’s assets and liabilities

### Overview

Efficient management of the Crown’s assets and liabilities contributes to improved overall economic performance through maximising the value of the Government’s investments and minimising the costs of the Government’s finance. The Treasury and CCMAU contribute by:

- monitoring performance and governance of organisations that are responsible for the day-to-day management of the Crown’s assets and advising Ministers on policy and strategic issues
- managing, through the New Zealand Debt Management Office (NZDMO), the Crown’s sovereign-issued debt and associated financial assets
- providing primary policy advice and, in some cases, managing commercial and contractual claims against the Crown.

In June 2004, the Crown owned \$110 billion in total assets, more than any other entity in New Zealand. These included equity interests in SOEs, Crown companies and CRIs, a number of other Crown entities and the financial assets accumulating in CFIs. The Crown’s assets are expected to grow to over \$145 billion by 2009, with the biggest change being the growth in assets held by the New Zealand Superannuation Fund (NZSF) to pre-fund future pension liabilities.

The Crown’s total liabilities in June 2004 were around \$75 billion, of which some \$35 billion was gross sovereign debt. Over the medium term, gross debt is forecast to remain close to this level in nominal terms, but to decline to around 20% of GDP by 2009.

The Crown's assets provide a resource to help meet future expenditure commitments and claims on the Crown, and income streams that reduce tax pressure in future years. Sustaining their value is important. By the same token, government debt creates costs and risks for the Crown that need to be managed. The Crown also faces other financial risks arising from contractual and commercial claims. These too need to be monitored and managed, consistent with the Crown's overall economic and other policy objectives.

#### Our desired outcome contribution

- Delivering operational outputs as required by Ministers, including continually improving our efficiency and effectiveness.
- Maintaining a high-quality capability to undertake commercial negotiations, transactions and risk management when this is demanded by Ministers.
- Continually looking to sustain and improve entity performance in a dynamic environment.

#### Our progress

##### State-owned enterprises

At the start of the year, we noted the importance for this outcome of continuing to apply long-term ownership principles to SOEs to ensure their performance and investment strategies meet Government objectives. Alongside our core activities of providing shareholding Ministers with advice on SOE and Crown company business plans and statements of corporate intent, and on a range of specific company issues, in 2004/05 we also concluded four strategic ("long-term hold") reviews of SOEs and progressed three others in consultation with the respective boards and management teams. These exercises have established, among other things, credit-rating benchmarks and have in each case clarified shareholding Ministers' preferences regarding thresholds for consultation on significant strategic issues.

##### Crown Financial Institutions

Another priority has been to improve our understanding of the Crown's financial assets, as they come to dominate the Crown's balance sheet. To this end, we have provided advice throughout the year on CFI performance, including investment returns, appointments, statements of intent, and a range of specific issues. This included managing a process for an independent review of the operation of the NZSF. The Fund's rate of return in 2004/05 was 14.13% (after costs, but before tax), well ahead of its benchmark targets and the rate achieved in the previous year.

##### Physical assets

The Treasury also conducted an internal stock-take of the Crown's physical assets, the majority of which are held by Crown entities, as a starting point for building effective asset and liability management into the Treasury's contribution to wider efforts to enhance governance and monitoring of Crown entities.

### Long-term hold reviews of SOEs

In 2003 the Government completed a review of the governance arrangements for SOEs in light of its policy not to sell State assets. It concluded the principles of the SOE Act were satisfactory but that there was a need to spell out more clearly Ministers' expectations in their role as shareholders. To this end it was decided to review all 16 SOEs (excluding Electricity Corporation of New Zealand Ltd and New Zealand Railways Corporation Ltd) in order to:

- be clearer with boards about shareholder expectations
- provide shareholders with a better understanding of SOE performance
- develop commercially appropriate capital structures
- ensure major SOE investments were considered relative to other demands on Crown capital.

During 2004/05 the Treasury and CCMAU assisted Ministers in completing long-term hold reviews of Landcorp Farming Ltd, Meridian Energy Ltd, Solid Energy New Zealand Ltd and Meteorological Service New Zealand Ltd. This brings the total number of reviews completed to six. The reviews were carried out jointly with the SOEs and covered the scope of business and consultation expectations, company performance, financial strategy and capital management.

These reviews enabled shareholding Ministers to clarify their expectations for each SOE. They were communicated to the boards of each SOE in a Statement of Shareholder Preferences. However, boards are independent of government and must decide for themselves on the way in which those expectations are used, consistent with the best interests of the company.

### Debt management operations

Improving our delivery of debt management outputs in 2004/05 was achieved through a wide range of activities. In the domestic market we issued \$2,150 million of Government bonds to meet the Government's funding requirement and completed \$1,150 million of New Zealand dollar interest-rate swaps.

We completed \$22 billion of foreign-currency transactions (including foreign-currency swaps) for the NZSF, and provided loans and issued \$1 billion of bonds as a capital injection to the Reserve Bank under new funding arrangements to support the Bank's foreign currency intervention capability.

We introduced new products, analytical tools and system improvements to enhance our ability to fund the Government's borrowing requirements, manage the stock of debt and add value, while balancing cost and risk objectives. Notably, we:

- executed a new two-year pricing agreement with the Guardians of NZSF to hedge their foreign currency exposures in up to 13 currencies
- concluded the re-negotiation of the Crown's transactional banking contract with Westpac, executed the domestic transaction banking services Master Agreement, and secured a three-year fixed-pricing arrangement for these banking services

- completed the transition of registry services provision from the Reserve Bank to Computershare Investor Services
- continued to develop proposals for infrastructure bonds to fund transport investments, including borrowing by Transit New Zealand to support the ALPURT B2 toll road.

### Efficient management of the Crown's debt

There are many influences on actual results, such as the overall level of debt, the level and evolution of market interest rates, the volume of intermediation and advances to parts of the Crown, and NZDMO's discretionary decisions. In some cases we made a direct contribution, while in others it was second-order. Outlined below is information on performance for the past three years.

Outcome Indicators	2001/02	2002/03	2003/04	2004/05
Core Crown finance costs on debt (\$m)	2,324	2,478	2,260	2,239
Value added in the foreign-currency portfolio (\$m)	6.5	13.4	7.9	23.5
Value added from NZD interest-rate swaps (\$m)	5.0	6.2	7.3	35.8
Adherence to policies and controls for managing risk, with nil material breaches	✓	✓	✓	✓

### Other commercial assets and claims against the Crown

The Treasury has continued to manage a number of the Crown's commercial assets and contractual functions, and also risks on behalf of the Government. We concluded the sale of the Crown's interests in Tarawera Forests Ltd; substantially completed negotiations to transfer the Crown's geothermal interests to Mighty River Power Ltd; provided advice on a number of historic Treaty of Waitangi settlement negotiations, and on wider policy settings; and provided advice to Ministers on the expansion of New Zealand Railways Corporation Ltd's role as it became the track operator, and on other rail-related issues. We also continued to operate the Export Credit Office, which in 2004/05 completed its second transaction and conducted a selection process to appoint a new professional agent to succeed EKF.

### Challenges ahead

As reported in our SOI for 2005/06, there are challenges and opportunities ahead. For 2005/06 our primary focus will be on continuing to deliver our operational responsibilities as efficiently and effectively as possible. In addition, we will be aiming to broaden and deepen understanding across the Treasury of asset and liability management issues, with a view to leveraging higher performance from the Treasury's ongoing and planned engagements with departments and agencies. We will strive to maintain and enhance our relationships with agencies and businesses that we monitor, and to improve our tools and capabilities for lifting performance by contributing to policy options for strengthening governance

arrangements, enhancing the quality and availability of performance information, and supporting high-quality monitoring.

We will also maintain our efforts to ensure that our policy frameworks remain fit for purpose as the composition of the Crown's balance sheet changes over time. We will investigate areas where changes to balance sheet management policies are likely to lead to material improvements in fiscal or economic outcomes, taking into account institutional and practical operational constraints.

### Crown agencies for which either the Treasury or CCMAU has lead monitoring responsibility

#### SOEs (CCMAU lead, and the Treasury)

- AgriQuality Ltd
- Airways Corporation of New Zealand Ltd
- Animal Control Products Ltd
- Asure New Zealand Ltd
- Electricity Corporation of New Zealand (Residual) Ltd
- Genesis Power Ltd
- Landcorp Farming Ltd
- Learning Media Ltd
- Meridian Energy Ltd
- Meteorological Service of New Zealand Ltd
- Mighty River Power Ltd
- New Zealand Post Ltd
- New Zealand Railways Corporation Ltd
- Quotable Value Ltd
- Solid Energy New Zealand Ltd
- Timberlands West Coast Ltd
- Transmission Holdings Ltd
- Transpower New Zealand Ltd

#### Other Crown companies

(CCMAU lead, and the Treasury)

- New Zealand Venture Investment Fund Ltd (VIF)
- Radio New Zealand Ltd
- Television New Zealand Ltd (TVNZ)

#### CRIs (CCMAU lead, and the Treasury)

- AgResearch Ltd (AgResearch)
- Industrial Research Ltd (Industrial Research)
- Institute of Environmental Science and Research Ltd (ESR)
- Institute of Geological and Nuclear Sciences Ltd (GNS)
- Landcare Research New Zealand Ltd (Landcare Research)
- National Institute of Water and Atmospheric Research Ltd (NIWA)
- New Zealand Forest Research Institute Ltd (Forest Research)
- New Zealand Institute for Crop and Food Research Ltd (Crop and Food Research)
- The Horticulture and Food Research Institute of New Zealand Ltd (HortResearch)

#### Other (CCMAU lead, and the Treasury)

- Air New Zealand Ltd (Treasury only)
- Christchurch International Airport Ltd
- Dunedin International Airport Ltd
- Invercargill Airport Ltd
- New Zealand Lotteries Commission (CCMAU only)
- Pacific Forum Line Ltd (CCMAU only)
- Public Trust

#### CFIs (the Treasury only)

- Earthquake Commission
- National Provident Fund
- New Zealand Superannuation Fund (NZSF)
- Government Superannuation Fund (GSF)

(Source: *Statement of Intent 2005/06*)

### Tackling trans-Tasman banking issues

In February 2005 the Australian Treasurer, Mr Peter Costello, and New Zealand Finance Minister Dr Michael Cullen announced the establishment of a Joint Trans-Tasman Council on Banking Supervision.

“The Australian and New Zealand banking markets are among the most highly integrated in the world. Given this high degree of commercial integration, there is benefit in moving toward seamless regulation in this area in order to minimise regulatory hurdles,” the Ministers said.

“We are determined to maintain momentum towards this goal while seeking to improve the quality and reduce the cost of regulation in both countries.”

The Council is chaired jointly by the Secretaries to the Treasuries of Australia and New Zealand, and also comprises senior officials from the Australian Prudential Regulation Authority, the Reserve Bank of Australia and the Reserve Bank of New Zealand.

The role of the Council is to promote a joint approach to trans-Tasman banking supervision that delivers a seamless regulatory environment. In particular the Council aims to:

- enhance cooperation on the supervision of trans-Tasman banks and information-sharing between respective supervisors
- promote and review regularly trans-Tasman crisis response preparedness relating to events that involve banks that are common to both countries
- guide the development of policy advice to both Governments, underpinned by the principles of policy harmonisation, mutual recognition and trans-Tasman coordination.

Since the establishment of the Council, Treasury staff have been working with other officials in New Zealand and Australia to progress the Council’s work.

Our ongoing focus on trans-Tasman banking issues is a good example of a workstream that supports a number of the Treasury’s key outcomes. Its focus is on a stable and sustainable macroeconomic environment, and it also contributes to more efficient and effective use of State resources and regulatory powers.

Working on trans-Tasman banking issues –  
Kerryn Fowlie (Treasury),  
Margaret Griffin (Reserve Bank),  
Jeremy Corban (Treasury),  
Stuart Irvine (Treasury) and  
Adrian Orr (Reserve Bank)



# ORGANISATIONAL STRUCTURE – THE TREASURY

**Responsible Minister:**  
Minister of Finance

**Vote Minister:**  
Minister of Finance

**John Whitehead**  
Secretary to the Treasury

Branch Managers/Deputy Secretaries

**Mike James**

**Asset and Liability Management Branch**

- Public Sector Management
- Crown Debt Management
- Crown Company Performance
- Crown Risk & Liability Management

**Peter Bushnell**

**Budget and Macroeconomic Branch**

- Budget Management
- Macroeconomic Policy Advice
- Macroeconomic Forecasting & Monitoring
- Fiscal Forecasting & Reporting
- Accounting Policy Development

**Iain Rennie**

**Regulatory and Tax Policy Branch**

- Tax Policy
- Regulation & Vote Purchase, Ownership & Performance Issues [Market Interventions, Environment & Natural Resources, International Economics & Defence, Revenue Agencies & Other Government Services]

**Peter Mersi**

**Social Policy Branch**

- Regulation & Vote Purchase, Ownership & Performance Issues [Health, Education, Welfare, Labour Markets, Justice Agencies, Māori Affairs & Other Population Agencies]

**Angela Hauk-Willis**

**Corporate Branch**

- Corporate Services
- Policy Coordination & Development

**Vote Ministers:**  
Minister for Crown Research Institutes  
Minister for State-Owned Enterprises

**Murray Wright**  
Executive Director

**Crown Company Monitoring  
Advisory Unit**

- Crown Research Institutes' Monitoring
- State-Owned Enterprises' Monitoring
- Appointments & Governance

# THE TREASURY – VISION AND MANAGEMENT OBJECTIVES

## Our vision

A world-class Treasury working for higher living standards for New Zealanders

## Our management objectives (T-I-M-E)

Our four management objectives summarise how we're going to achieve our vision:

### T Take the lead

- Shape the economic agenda and proactively identify new areas of opportunity.
- Anticipate ministerial needs and issues for the future and position ourselves to improve advice on key Government priorities.
- Respond quickly and innovatively to changing demands and circumstances.

### I Invest in our organisation and its people

- Encourage and develop effective leadership.
- Enhance the capability of our people, addressing any talent gaps to support our outcome priorities.
- Develop the systems, structures and processes required to become a more flexible and capable organisation.

### M Manage for outcomes

- Achieve results in the outcome areas where we know we can make a difference, through harnessing our collective capability.
- Achieve effective use of resources, by ensuring maximum focus in the areas of highest priority.
- Achieve continuous improvement in our core areas of business, through stretching and working smarter.

### E Engage effectively

- Consistently communicate a clear Treasury vision across the organisation.
- Work together as “one Treasury” in order to provide integrated policy advice to the Minister and Government.
- Develop strong external relationships that enable us to provide high-quality advice and deliver on our responsibilities in the most effective way.

## MAINTAINING AND DEVELOPING CAPABILITY

Over the past year, we've continued to focus on maintaining and developing the Treasury's capability, so we can provide even better economic and financial advice to Ministers. The T-I-M-E management objectives outlined on the previous page provide us with a broad framework for doing this.

### Taking the lead

#### Overview

The Treasury's role requires it to work across a very broad range of areas. This in turn makes it a real challenge for us to cover the areas we need to cover, and respond swiftly to emerging issues, while still anticipating emerging issues and meeting changing ministerial needs.

A main focus for us has therefore been on how we can position ourselves to best help Ministers shape economic and fiscal strategy.

We also assessed our ability to deliver on our outcome priorities, using a series of cross-Treasury discussions. Secretary to the Treasury John Whitehead briefed staff on the issues and proposed actions in June 2004. Project planning is now underway, in particular looking at how we can improve our focus on managing for outcomes in planning for 2005/06.



Senior managers –  
Peter Bushnell, Peter  
Mersi, John Whitehead,  
Angela Hauk-Willis,  
Mike James, Iain Rennie

### Our management objectives

- Shape the economic agenda and proactively identify new areas of opportunity.
- Anticipate ministerial needs and issues for the future and position ourselves to improve advice on key Government priorities.
- Respond quickly and innovatively to changing demands and circumstances.

### Indicators signal where the economy is heading

One of the Government's key objectives is to improve the living standards and wellbeing of all New Zealanders in a sustainable way. But how do we know if we are making progress?

One way is to use a range of indicators to monitor New Zealand's progress towards its economic goals, while benchmarking our performance against other countries in the OECD. That is exactly what a joint project between MED and the Treasury set out to achieve.

*Economic Development Indicators 2005* brings together indicators from a range of national and international sources to provide a comprehensive picture of the New Zealand economy. It measures a range of outcomes and growth determinants, including material standards of living, labour utilisation, productivity, investment and innovation. Its main purpose is to inform future economic policy and, as part of that, provide a basis for engaging with New Zealanders over economic policy development.

Information for the report, which was published in February, was gathered over several months by a joint Treasury/MED team. The report shows that while New Zealand's economy has performed well in recent years, there are future challenges that need to be considered, such as low levels of labour productivity, skills shortages and relatively low levels of business investment.

A follow-up report is expected to be published in two or three years, once sufficient time has passed to allow a worthwhile assessment of overall progress.

The Treasury and MED have a shared interest in the performance of the economy, as evidenced by the joint production of the report. MED's Five Strategic Priorities for Growth are aimed at strengthening New Zealand's business environment and promoting innovation, while economic growth is one of five key outcomes for the Treasury.

Both organisations hope the publication will provide the basis for a sustained dialogue on how best to address the challenges it highlights, and further improve New Zealand's economic performance.



Julia Hall worked on the *Economic Development Indicators 2005* report

### Preparing the post-election briefing

Each election year the Treasury prepares a briefing paper to the incoming government. This post-election briefing is to inform Ministers of the major issues that the Treasury sees facing New Zealand over the next few years. The briefing involves drawing together advice and analysis from across the Treasury's policy branches to make sure the key issues are identified and highlighted for Ministers. This involves a lot of internal discussion, and scrutiny of available evidence and theoretical literature.

Key challenges outlined in the 2005 post-election briefing are:

- further enhancing New Zealand's economic growth
- maintaining fiscal stability
- lifting the performance of the public sector.

The project starts well before an election date is announced, and this year was led by Struan Little and Anna Cook, with support from Lisa-Marie Cowley.



The post-election briefing project team – Anna Cook, Struan Little and Lisa-Marie Cowley

### Our progress

The development of our strategic direction over the past year helped give us a clearer sense of what our overall priorities are, and therefore where we should be putting the most effort over the next few years.

During the year we undertook several initiatives that demonstrated our ability to provide leadership as an organisation.

Examples include our work with MED in producing the *Economic Development Indicators 2005* document, and organising productivity and labour participation workshops.

We continued to undertake research on topical economic issues, and to use the knowledge gained to inform policy debates. In 2004/05 we reviewed our publications and introduced a new suite of publications: a Treasury Papers series, which will be Treasury-authored and express our view on issues; and a

new Treasury Policy Perspectives series, authored by individuals and focused on releasing more immediately policy-relevant work in an accessible format. These two new series sit alongside our Working Papers publications series.

During the year we released 23 working papers and three policy perspective papers. We continued to use invitations for external presentations and internal seminars to disseminate Treasury work more widely. Our guest lecture series enabled us to hear a variety of perspectives on relevant issues. All these things help to promote internal debate and discussion about critical financial and economic issues, and to bring external perspectives to bear on these as well.

There were several instances during the year when we had to respond quickly when faced with changing circumstances. This includes our intensive work on the Budget savings initiatives, the tax depreciation changes and the tax treatment of financial intermediaries.

More proactively, the Treasury initiated work on health sector performance and productivity, as well as expanding our analysis of fiscal trends and their drivers in anticipation of dealing with mounting fiscal pressures.

### Challenges ahead

This is an area where we need to keep improving our ability to show leadership and to work strategically and responsively. To do this, it is imperative that we try to find ways to avoid our day-to-day work crowding out our capacity to think longer-term and our responsiveness to ministerial demands.

## Managing for outcomes

### Overview

In 2004/05, our main focus was on taking our 2003/04 direction-setting further, drawing in our business-as-usual work, and moving into detailed planning and implementation.

#### Our management objectives

- Achieve results in the outcome areas where we know we can make a difference, through harnessing our collective capability.
- Achieve effective use of resources, by ensuring maximum focus in the areas of highest priority.
- Achieve continuous improvement in our core areas of business, through stretching and working smarter.

### Our progress

During 2004/05 we have put a lot of effort in this area, building a commitment to managing for outcomes within the organisation, developing a clearer sense of strategic direction and updating our planning and reporting processes to support it.

By integrating post-election planning, planning and strategic Vote assessment work, we drew staff into thinking about managing for outcomes and provided a common basis for developing an agreed strategic direction and outcome plans for the organisation.

We encouraged a conversation-based approach, from senior managers collaboratively reviewing broad outcome plans, to staff debating more detailed work priorities in their teams and sections. This has enabled us to better link strategy, in the form of agreed outcome plans, to resource allocation and detailed work plans.

This new approach to planning has been complemented by a new process for assessing our performance. Introduced in March, this process involves a more systematic organisation-wide review of progress against our stated priorities three

times a year. As well as giving us a better shared sense of overall progress, it has also helped us get better at reprioritising resources.

In terms of our financial management, we aim for a 0% to 3% year-end underspend – this encourages us to budget and prioritise effectively and to make effective and efficient use of the resources available to us, while not exceeding our appropriation. As the figure illustrates, we have steadily improved our performance in this area. During 2004/05 we returned \$1.8 million to the Crown and reprioritised

our work to support new initiatives, such as in-depth reviews on public sector productivity and innovation.

### Challenges ahead

An ongoing challenge will be to ensure the Treasury is able to respond quickly and be flexible in moving resources to areas of highest priority. There are also tensions in planning, delivering and reporting on work across outcome, output class and Treasury branch boundaries. During 2005/06 we will review our output class structure and also aim to streamline our management of outcomes and cross-Treasury projects.

Looking ahead, we also see potential for us to work more collaboratively with other agencies on shared outcomes, especially working with other central agencies to improve public sector effectiveness.

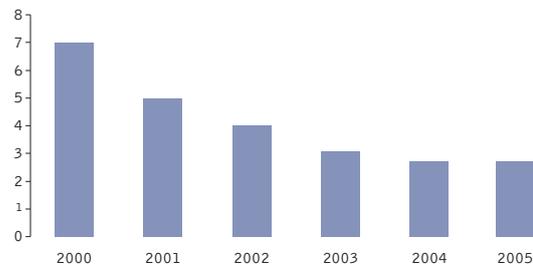
## Investing in our organisation and its people

### Overview

Our success depends on maintaining and developing a talented workforce and making full use of their experience and expertise.

### VOTE FINANCE - FINANCIAL OUTTURN VERSUS BUDGET

% variance at 30 June



### Our management objectives

- Encourage and develop effective leadership.
- Enhance the capability of our people, addressing any talent gaps to support our outcome priorities.
- Develop the systems, structures and processes required to become a more flexible and capable organisation.

### Our progress

#### Changing staff profile

The Treasury employed 320 staff at the end of June 2005, an increase from 312 the previous year. We also seconded a further 11 staff to various agencies, employed one wage worker and had 28 staff on leave without pay, including parental leave.

The average length of service decreased from 6.4 years in 2003/04 to 6.2 years as at 30 June 2005, and the proportion of staff staying more than one year decreased from 92% at 30 June 2004 to 84% this year. The profile for our economic and financial analyst staff has shifted over recent years, with an increasing proportion of analysts in senior analyst and principal advisor roles.

Staff turnover was 13.2% compared with 11.4% last year.

Over the past three years we have experienced low turnover in comparison with the 20%-plus levels of the previous years. We will continue to monitor turnover and seek to identify the factors driving change.

#### EEO progress

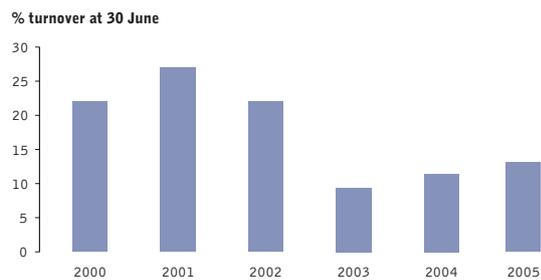
In June 2000, the Treasury set itself indicative forecasts for employing more women, Māori and Pacific Island people over the next five to 10 years.

The percentage of women in the Treasury has increased over recent years to 48% at the end of 2004/05. The percentage of women in senior management has also increased to 36.7%, exceeding the 28% level we forecast for 2010.

Māori comprise 6.3% of Treasury staff, with Pacific Island people representing a further 2.8%. This is in line with our indicative forecasts for 2005 (6.4% for Māori, 1.9% for Pacific Island people).

We have continued to implement an EEO Management Programme designed to make the Treasury's culture more supportive, ensure all staff are valued for the contribution they make, and

**TREASURY STAFF TURNOVER**



**TREASURY EEO 2005**



encourage target group staff to join, remain with and develop within the Treasury. Key achievements during 2004/05 were:

- a series of sessions to provide ongoing development for the Treasury's EEO consultative committee members
- hosting the Wellington launch of the Diversity Game, a tool that assists organisations to understand their obligations and think laterally about ways of meeting both business and individual needs around work/life balance and other EEO issues
- holding a work/life balance "issues and options" session with the EEO Trust.

These initiatives have all helped to profile the organisation internally and externally as a good EEO employer, and ensure that the Treasury has the internal skills and understanding to support this.

### A smarter approach to learning and development

Like any organisation, a highly skilled and motivated workforce is critical to the achievement of the Treasury's strategic goals.

Last year, the Treasury developed a new strategic direction for the next five years. In line with this direction, a project team was established to identify any gaps in the current capability of the Treasury's people, and to develop solutions to address these.

"Treasury people tend to be well qualified, and many have worked here for a number of years, so it was no surprise to find that our current staff capability was already pretty good," said project leader Kathryn Fraser. "However, the team identified several gaps in our technical capability, management or leadership capability, and relationship management and communication skills that needed to be addressed."

The team recommended a number of programmes, including a four-tier approach to developing employee knowledge in key subjects such as economics, law, accounting and business; a leadership and staff management programme specifically targeted to meet individual needs; and a range of learning and development activities to help staff develop their communication and relationship management skills.

The lack of a common approach to learning and development across the Treasury was also of concern. "Until now, each branch has been responsible for its own learning and development activities, which in some cases has led to mixed results," said Kathryn. "That's why we recommended the Treasury establish a central Development Centre, which will have overall responsibility for the management and coordination of our learning and development programmes."

The Development Centre will be complemented by three capability advisory groups, made up of employees from each branch, who will provide essential input into the development and delivery of Treasury programmes.

The roll-out of the new framework is expected to be completed within the next two years.

### Our Graduate Recruitment Programme

Each year our Graduate Recruitment Programme brings new faces and fresh thinking to the Treasury. The programme attracts graduates from a range of academic disciplines, who possess an incisive, questioning intellect and enjoy open and lively debate while operating in a challenging environment.

During 2004/05, 11 Graduate Analysts joined the Treasury in one of our five branches. Upon joining the Treasury, Graduate Analysts are immediately involved in a wide range of important work areas, such as working with and providing advice to other government departments. We provide Graduate Analysts with responsibility for their own portfolio of work and ensure they are well supported within a positive working environment where they are encouraged to develop and grow their skills and capability.

A key component of the success of our Graduate Recruitment Programme is the ability to offer promising career paths to our Graduates. Graduate Analysts work with their managers to create a personal development plan that will assist them in achieving their personal and career goals and which aligns with the Treasury's key objectives. Learning and development opportunities include a variety of work and training options, coaching, study, rotation within the Treasury and secondments to other organisations.

Diversity, fresh ideas and new perspectives are just some of the many benefits that the Treasury receives from recruiting graduates. The Graduate Recruitment Programme continues to be an important investment in our organisational capability.

### Encouraging and developing effective leadership

During 2004/05, the Senior Managers' Group reviewed the Treasury's senior staff capability and established a project team to make recommendations to clarify senior roles and career paths. The project team reported back early in November 2004. Decisions were aimed at "populating" the spectrum between managers and technical specialists; getting more people operating with a broad field of vision; and freeing up senior people more readily for priority discretionary work. The first of those proposals involved revamping the responsibilities of 14 senior staff and establishing new roles for them as directors, in addition to clarifying and refocusing other senior roles.

We have also been using cross-Treasury projects to provide opportunities for senior staff to provide leadership on priority pieces of work.

While we have started to see some behavioural change associated with the above initiatives, we expect that this change is likely to happen over the medium rather than short term.

### Treasury employees recognised for impressive accomplishments

The Treasury employs people who excel in a broad range of fields, and several of our top achievers were recognised for their professional, academic, sporting and community accomplishments during 2004/05.

Grant Scobie received the New Zealand Institute of Economic Research's Economist of the Year Award for 2004/05. The award recognised Grant's recent work on population ageing and retirement savings, as well as his earlier work on agriculture, trade, and research and development.

Nathan McLellan was voted onto the Council of the New Zealand Association of Economists. A member of the Association for six years, Nathan works with others in the Council to promote the Association's aims. This work includes promoting collaboration and discussion among professional economists in New Zealand; encouraging economic research; and fostering in all sections of the community an understanding of New Zealand economic problems.

Iris Claus graduated with a PhD in Economics from Victoria University. Iris' thesis assessed the effects of credit market borrowing and lending in a small open economy. Well-functioning credit markets lower the costs of borrowing and increase a country's capacity to produce goods and services. Because of the importance of credit markets in an open economy such as New Zealand, Iris concluded that it is important to extend models used by policy-makers to include credit markets.

Also graduating from Victoria University during the year was Ronda Sangster, who received a Master of Commerce and Administration. Ronda's thesis was on establishing the links between people capability and outcomes in the New Zealand public service environment.

Nikki Edwards completed her part-time study for the legal professionals course and was admitted to the Bar as a Barrister and Solicitor.

Lesa Laga made the New Zealand Women's Volleyball team again in 2005. She has been a member of the team since 2003, and has represented New Zealand at the Asian Women's Volleyball Champs in Vietnam (2003) and the Oceania Champs in Tahiti (2004). Lesa is also Captain of the New Zealand Institute of Sport Women's Volleyball team.

Julia Hall has been selected for the New Zealand national korfbal squad. This squad will form the basis of the team that is expected to take New Zealand to success at the Asia Oceania Korfbal Championships in Hong Kong in July 2006.

When not working at the Treasury, Wayne Stevens can sometimes be found dangling from



helicopters or coordinating search and rescue operations in tough terrain. Wayne's two decades of experience has been recognised with his appointment as an advisor to the Wellington region Police commander for search and rescue. In January 2005, Wayne was part of a team that spent two nights in rough bush and terrible weather rescuing a trumper from the top of the Southern Crossing in the Tararuas.

In other achievements of note, Treasury staff produced a number of significant external publications during 2004/05, including:

- Grant Scobie and John Bryant (with Ross Guest of Griffith University, Australia), "Population Ageing in New Zealand: Implications for Living Standards and the Optimal Rate of National Saving", *New Zealand Economic Papers*, Volume 38, Number 2, 2004.
- Bob Buckle (with David Haugh of Australian National University and Peter Thomson of Statistics Research Associates Ltd, Wellington), "Markov Switching Models for GDP Growth in a Small Open Economy: The New Zealand Experience", *Journal of Business Cycle Measurement and Analysis*, Volume 1, Number 2, 2004.
- Brian McCulloch and Jane Frances, "Governance of Public Pension Funds: New Zealand Superannuation Fund" in Musalem, A and R Palacios (eds.), *Public Pension Fund Management: Governance, Accountability and Investment Policies* (Washington DC: World Bank, September 2004).

### Enhancing the capability of our people

Treasury staff have high expectations about their opportunities for ongoing career development. The 2004 Treasury Climate Survey showed staff perceptions of career opportunities had improved, after a dip in 2002. There was less improvement on professional growth, but we score well above the external benchmark on both, with 61% of staff positive about career opportunities (30% benchmark) and 67% positive about professional growth (55% benchmark).

The one area that the survey identifies where we do not do so well is job satisfaction. This is the single area where we rank lower than the external benchmark. Through branch discussion and focus groups we are getting better clarity on the factors underlying the job satisfaction figures, to help us identify any steps we should be taking during 2005/06.

As part of our commitment to staff training and ongoing professional development, we spent \$2,320 per head on formal staff training during 2004/05. This significantly understates our investment, as it does not capture on-the-job training, which is highly valued by staff and provides a high return to the organisation. During 2004/05, 262 staff reported an average of 39 hours spent as "training received" and/or part-time study. Promotion and staff rotation have also provided fresh challenges and new opportunities for staff. We also continue to have a number of staff on secondment to other organisations such as Ministers' offices.

Learning and development initiatives that have been run during the year include:

- workplace bullying – four sessions
- change management – for managers
- providing a new Māori Responsiveness course
- reviewing some targeted senior staff development needs
- developing and implementing a new manager "toolkit"

- a new in-house course on relationship development
- the establishment of a more structured approach to considering senior staff capability
- the development of a data base of learning and development service providers.

In 2004 we identified the need for a more general look at staff capability to support the Treasury's review of its strategic outcome direction over the next five years. This was to identify and address any gaps in resources to ensure that we are able to achieve our outcome goals. A cross-Treasury project team reported back with recommendations in March 2005. As a result of this work, we have agreed to shift some of the responsibility from our five branches and establish a centralised Development Centre. This will provide for more targeted and prioritised resourcing of specifically identified development needs, and the design and delivery of learning and development programmes that will be coordinated across the Treasury. The programmes will provide for structured and progressive learning for staff and will be delivered through a variety of differing learning media.

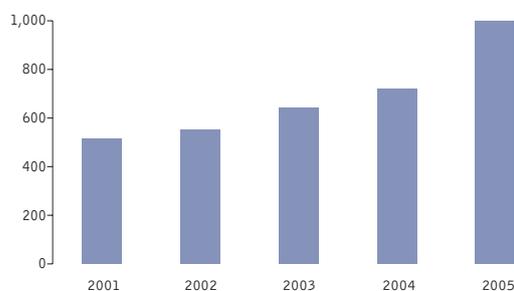
#### Enhancing organisational systems, structures and processes

With personnel costs representing approximately 65% of our total expenses, good human resource information is vital. During 2004/05 we identified a preferred supplier for a new payroll and human resource information management system, which we aim to introduce during 2005/06.

The refurbishment of our accommodation at No. 1 The Terrace has been a major project over the past two years. The final stage was completed by January 2005, with all Treasury staff relocated to refurbished accommodation on floors 5 to 14. The project finished on time and on budget and provides us with a flexible, modern workplace that should meet our long-term needs. It has also meant that we have been able to reduce our accommodation costs over the years ahead.

We have continued to focus on capturing the benefits from our investment in knowledge management systems and promoting good knowledge management behaviour.

#### MINISTERIAL CORRESPONDENCE



We provided staff with a set of intranet portal tools to integrate access to information and services, tailored to meet individual needs based on roles or team membership. The portal is a flexible platform which positions us to use collaborative workspaces and a range of sophisticated techniques to support core business processes.

We improved online access to the most relevant external information sources throughout the year, and trained many staff to use them effectively. We also increased our level of support for flexible working arrangements, such as remote computing access.

During the year we have seen a significant increase in the volume of ministerial correspondence. We have reviewed our tracking systems, revised our reporting standards and provided some additional resources to enable us to better meet the demand for this work.

### The write staff

The ministerial team is made up of the ministerial writers and the ministerial coordinator. Collectively, they are responsible for replying to ministerial correspondence and processing all documentation between the Treasury and the Ministers' offices. They work closely with the Minister of Finance's office to track documents and reply to the huge amount of correspondence received.

A steady increase in the volume of this correspondence has led to the development of the innovative Ministerial Text System (MINTS), an information technology tool that will make it easier for our writers to find, store and reuse document fragments in ministerial replies. MINTS will reduce the time taken to draft responses, improve accuracy and consistency of replies and ensure we provide the most current information. Other government agencies have already shown strong interest in the system. The efficiency gains possible from MINTS could be significant if the technology can be applied widely across the public sector.

With increasing public demand for government information and higher public expectations of responsiveness from government agencies, the ministerial team will remain focused on the challenge of improving performance on timeliness and quality standards.



The ministerial team – Robin Gebbie, Rohan Light, Annette Kennedy, Kevin Hillock and Helen Denham

### Challenges ahead

The key challenge ahead is to continue initiating and bedding in behavioural change, which can be a difficult task. Behaviours we are encouraging include relationship-building inside and outside the Treasury, free and frank discussion, and better sharing and promoting of ideas that are important for the Treasury. Senior staff behavioural change is taking time and we are aiming for increased momentum in this area. An additional challenge is managing the risks in establishing the Development Centre and Human Resources information system. We are also focused on refreshing the capability of our staff in a lower turnover environment.

## Engaging effectively

### Overview

Engaging effectively both within the Treasury and with our external stakeholders continues to be a priority. Our strategic direction work has helped us to be more coordinated and consistent in our staff communications, enabling us to better link our strategic direction initiatives and be clearer about how they fit into the overall picture. Externally, we are moving from an investment and capacity-building phase to a focus on bedding in our last two years' work.

### Our management objectives

- Consistently communicate a clear Treasury vision across the organisation.
- Work together as "one Treasury" in order to provide integrated policy advice to the Minister and Government.
- Develop strong external relationships that enable us to provide high-quality advice and deliver on our responsibilities in the most effective way.

### Progress

Our stakeholder relations activity has been guided by the outcomes set out in our stakeholder communications plan for 2004/05:

- Being perceived as an effective and influential policy ministry.
- Demonstrating leadership, and working cooperatively across the public sector.
- Having strong links to a wide range of stakeholders both within and outside Wellington.
- Having a reputation and internal culture that enable us to attract and retain staff with the skills and experience we need.

Over the past year, we have made steady progress in engaging more effectively with our internal and external stakeholders.

We identified and took up a number of speaking opportunities for the Secretary and other members of the senior management team. A growing proportion of these speaking engagements are generated proactively by the Treasury, which helps to ensure they are high value and well targeted to our stakeholder priorities. In addition, we undertook Auckland business visits that have helped us to start building some valuable links with this target stakeholder group.

The speaking engagements and business visits represent a significant step forward for us in terms of our outreach. We have also established a team to review and further improve the Treasury's relationships with the business sector. Over the next year we expect to see some of the benefits of these links flowing into our policy development work.

Our research and policy work was made regularly available as working papers on our internet site, and we promoted debate on policy implications through seminars, workshops and other channels. We also engaged directly with media on key work such as the productivity workshop and the 2005 Budget pre-briefing. Our cooperation across the public sector was demonstrated by our assistance with several E-Government initiatives, including the government Wide Area Network (WAN) proposal, the government certificate authority project and the secure computing steering group.

We continued to send regular email newsletters to Treasury alumni around the world, to develop and maintain links with former staff. A survey of the alumni programme received some very positive feedback and suggestions, which will assist us in implementing improvements during 2005/06 to make the programme even more effective.

Our internet site ([www.treasury.govt.nz](http://www.treasury.govt.nz)) remains a key source of information for our stakeholders. During the year we launched a news feed service on the website to enhance the distribution of our published information. External and internal surveys and consultation have been undertaken as part of a wider review of our website, the benefits of which will flow through during 2005/06.

We placed a far greater emphasis on internal communications during 2004/05 – in support of developing an internal culture that helps us retain and develop our current staff. The implementation of the strategic direction has given us a good vehicle to deliver better-integrated, more consistent communications across the Treasury. Through a programme of guest lectures, internal seminars and reading group discussions, we have also kept staff well informed on issues of broad policy relevance.

### Challenges ahead

Our outcome-focused approach should make it easier to identify communications opportunities. However, we will need to ensure we capitalise on these opportunities by engaging earlier with key stakeholders to convey the Treasury's views on important issues.

We recognise there is further scope to engage with departments at a cross-Treasury level – particularly with the other central agencies. There is some shared planning activity proposed, which provides a potential opportunity for some coordinated engagement by central agencies with other departments. In addition, our planned stakeholder survey and publications review are both areas where we could look at collaboration with the other central agencies.

On internal communications, our challenge is to ensure that we are clear with staff about the implications of our outcome direction for their day-to-day work. We will also increase efforts into communicating internally on major projects.

### Reaching out to create good policy advice

Choose any issue on the Treasury's work programme – economic development to resource management, climate change, health, education, justice – and it is clear that issue affects many people, groups or organisations beyond the Treasury itself.

So delivering the best possible policy advice on these and many other wide-ranging topics requires links with a diverse range of stakeholders – both within and outside the public sector, Wellington and even New Zealand.

“It has been a very conscious decision on the Treasury's part to take a much more active approach to external engagement in recent years,” says Treasury Chief Executive John Whitehead. “The aim is to build our profile as the Government's primary source of expert economic and financial advice – as well as boost our ability to anticipate and lead on issues. Listening to and learning from stakeholders is very valuable to us in creating good policy advice.”

The Treasury's strategic direction identifies engaging effectively with stakeholders – both internally and externally – as one of four management objectives for the Treasury over the next three to five years.

In 2004/05, this has seen senior management taking a much more deliberate and planned approach to interacting with Auckland-based businesses and influencers. In particular, a large number of speaking engagements and less formal meetings have been held with priority stakeholders outside Wellington.

Other initiatives have included regular senior management media contact and media training for staff, improved ministerial and business stakeholder relations through respective cross-Treasury groups, and reviews of the Treasury's publications and website. The Treasury also contributed to the three-day Hui Taumata held in Wellington in March this year, where ideas for accelerating Māori economic development at local, regional, national and international level were discussed.

“Building up relationships with people outside our organisation who have an interest in issues we deal with – and who can contribute in many different ways – can only be good for the quality of our policy advice,” John says. “It's certainly a focus that is beginning to make an impact here at the Treasury.”

# ORGANISATIONAL RESPONSIBILITIES

The Treasury is led by John Whitehead, the Secretary to the Treasury, and comprises five branches. Each branch has a specific focus, however there is a great deal of interaction across the Department.

## Asset and Liability Management Branch

Mike James

The Asset and Liability Management Branch has both operational and policy advice functions. The Branch:

- manages the Crown's debt, overall cash flows and interest-bearing deposits through NZDMO
- advises Treasury Ministers on public sector financial management systems and managing commercial, contractual and litigation risks on behalf of the Crown. The Branch also provides policy advice on managing and negotiating Treaty of Waitangi claims
- advises on the Crown's ownership interests and obligations in respect to SOEs, Crown companies, Air New Zealand and CFIs.

## Budget and Macroeconomic Branch

Peter Bushnell

The Branch has three broad lines of work that include:

- advising the Government on Budget strategy, design, process and management; preparing fiscal projections and the Crown financial statements; and reviewing departmental financial management systems to provide assurance that there is a reasonable system of internal control
- monitoring the economic situation, preparing macroeconomic and tax forecasts and providing advice on macroeconomic policy
- advising on Crown accounting policies.

## Regulatory and Tax Policy Branch

### Iain Rennie

The Regulatory and Tax Policy Branch advises Ministers on regulatory issues with important economic consequences. These include environmental policy, competition and trade policy as well as transport, local government, land use and natural resources.

The Branch also advises on the structure and operation of a range of government departments and entities in these areas.

Tax policy advice covers the level and mix of direct and indirect taxes, the taxation of international income and the taxation of particular types and sectors of business.

## Social Policy Branch

### Peter Mersi

The Social Policy Branch advises Ministers on the purchase and regulation of social services and public goods, ranging from education and health services to labour market policies, social support services, housing and law enforcement. These are all areas involving a large share of government expenditure.

In addition to advice on spending proposals, the Branch reports on the budgets and financial performance of government agencies.

The Branch provides advice to give assurance to Finance Ministers about departmental proposals. It advises the Minister of Finance on policy developments in the area of social policy and often participates in interdepartmental working parties on reform proposals.

## Corporate Branch

### Angela Hauk-Willis

The Corporate Branch provides advice to the Chief Executive and senior managers on corporate strategy, policies and practices for the Treasury. The Branch also provides services and specialist advice in relation to finance and planning, human resources, risk management, communications, legal and knowledge management.

The Branch is also home to the Policy Coordination and Development unit (PCD). PCD's role is to maintain an overview across Treasury policy development, keep abreast of emerging ideas and research, and review and challenge existing Treasury thinking. PCD provides analysis and advice on medium-term strategy issues.

As at 30 June 2005 we had the following number of staff in each of the branches, compared with the previous year.

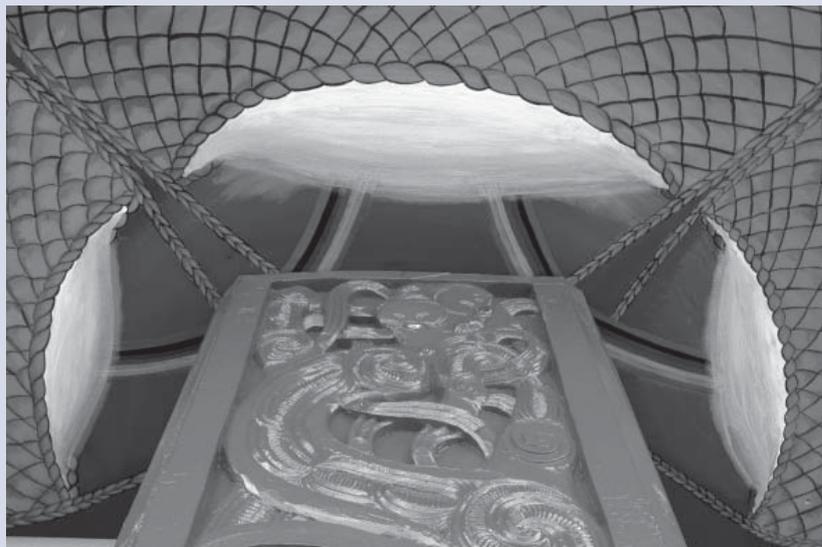
	2004	2005
Asset and Liability Management Branch	64	57
Budget and Macroeconomic Branch	47	57
Regulatory and Tax Policy Branch	56	62
Social Policy Branch	65	62
Corporate Branch*	80	82
Full-time Training	-	-
Total Treasury Staff	312	320

\* Corporate Branch includes the Secretary to the Treasury's office.

### The Treasury whareniui

The Treasury whareniui, Nga Mokopuna a Tane, is located on the 14th floor of No. 1 The Terrace. Nga Mokopuna a Tane means “the grandchildren of Tane”, which is an appropriate name given Tane’s prominence in both the room and in Māori and Pacific Island history.

The whareniui was first opened in 1991, and reopened again in 2004 following a major building refurbishment. It is used primarily for seminars and discussion/reading groups. It is also the place where we welcome new staff to Treasury with a powhiri.



## VOTE FINANCE AT A GLANCE

Actual expenditure for 2004/05 by output class



(Figures are GST inclusive)

# OUTPUT PERFORMANCE – VOTE FINANCE

Statement of Objectives and Service Performance  
section 35(3) Public Finance Act 1989

## Policy Advice: General Economic and Fiscal Strategies

This class of outputs involves policy advice on the Government's broad economic strategy and macroeconomic policy settings, and their effect on living standards for New Zealanders.

This includes advice for the Government on strengthening the fiscal policy framework and improving the framework for monitoring monetary policy outcomes.

General economic and fiscal strategy requires empirical and analytical research to support and inform policy advice. This output class includes research and policy advice with a medium-term perspective, taking account of the characteristics of the New Zealand economy. This research and policy advice will focus on how to improve New Zealand's economic performance, looking at growth, productivity and macro stability issues.

### Significant work completed during the year

- Helped the Government set out its strategy for the 2005 Budget in the *2005 Budget Policy Statement*, and published the Government's medium-term fiscal intentions in the *2005 Fiscal Strategy Report*.
- Planned, hosted and participated in International Monetary Fund and OECD missions to New Zealand, including preparing briefing material, answering follow-up questions and agreeing completed surveys.
- Led a group of departments (Treasury, MED and RBNZ) to organise and hold a major workshop "Productivity: Performance, Prospects and Policies".
- Reported to the Minister of Finance on critical issues for economic growth.
- Collaborated with MED to complete the *Growth through Innovation: Economic Development Indicators 2005* report for publication in February 2005.
- Published a range of working papers examining New Zealand's productivity performance and the impacts of adult literacy, financial systems, institutions and firms on economic growth.
- Reported to the Minister of Finance on what has been learnt from research on productivity.
- Advised Ministers on a package of reforms to improve support for business research and development.
- Provided support and advice around the re-negotiation of the Reserve Bank Funding Agreement.
- Published working papers on new evidence on saving for retirement and on household incomes in New Zealand.

### Service performance\*

Performance Dimensions	Achieved?
<b>Quality</b> <ul style="list-style-type: none"> <li>All reports will comply with the Quality Standards for Analysis and Advice. The Minister will be requested to indicate his level of satisfaction with the overall quality of outputs.</li> <li>Fiscal publications produced under this output class will meet the requirements of the Fiscal Responsibility Act 1994.</li> </ul>	Met and frequently exceeded expectations
<b>Quantity</b> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05.</p>	✓
<b>Timeliness</b> <p>All outputs will be delivered to timeframes as agreed between the Minister and the Secretary to the Treasury for 2004/05.</p>	✓

### Cost (\$000)

2004/05 Actual	4,469
Supp. Est - Voted	4,568
Main Est.	5,427
2003/04 Actual	3,983

(Figures are GST inclusive)

Actual 2004/05 output class expenditure was \$99,000 or 2% under Supplementary Estimates budgets.

The appropriation for this output class was decreased by \$859,000 in the Supplementary Estimates owing to several consulting projects not proceeding and lower accommodation project operating costs.

\* General service performance objectives are detailed on pages 71 to 72.

## Policy Advice: Financial and Public Sector Management Systems

This output class involves policy advice on financial and public sector management systems in use across the Crown and contributes to:

- improved decision-making and performance management systems that facilitate the effective and efficient use of State resources and regulatory powers
- efficient management of the Crown's assets and liabilities.

It covers the development and design of specific public sector management regimes applicable to departments and Crown entities. It also includes development of financial policy that takes into account the Crown's overall pattern of expenditure, revenue, assets, liabilities and risks, in order to minimise the economic costs through time arising from financing a given profile of government expenditure.

Outputs will specifically include advice on:

- the governance, incentives, operating framework and reporting systems for departments and Crown entities to ensure effective performance and accountability relationships between entities and their stakeholders
- the range and nature of financial risks to which the Crown is exposed and the degree to which these can be managed more efficiently when considered as part of an integrated set of risks, assets and liabilities across the Crown.

### Significant work completed during the year

- Provided policy and legislative support for the passage of the Public Finance (State Sector Management) Bill as the Public Finance Amendment Act 2004 and the Crown Entities Act 2004.
- Provided advice and support to Ministers, departments and Crown entities on the roll-out of the Crown Entities Act 2004, including:
  - guidance material on reporting requirements
  - bank account and debt securities approvals
  - delegations on guarantees and indemnities for departmental operations
  - a report to Cabinet on the Crown Entities (Financial Powers) Regulations 2005.
- Developed, with SSC, a Managing for Outcomes self-assessment tool, and revised *Statement of Intent* guidance for departments.
- Reported to the Minister of Finance on the operation of the departmental capital charge and the multi-year appropriation scheme.
- With SSC and DPMC, reported to the Minister of State Services on innovation in the public sector, and held follow-up forums for departments on enabling more innovation.
- Completed a review of non-government organisation (NGO) contracting arrangements and reported back to Cabinet.
- Developed a framework for identifying early warning signs aimed at improving the performance of agencies.

- Participated in a work programme to advance a “central agency” shared outcome aimed at improving the performance of the State sector.
- Completed a review of the rate of return assumptions to be applied to CFIs.
- Completed work measuring the risk and return properties of the Government’s overall balance sheet.

Service performance\*

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <p>All reports will comply with the Quality Standards for Analysis and Advice. The Minister will be requested quarterly to indicate his level of satisfaction with the overall quality of outputs.</p>	<p>Met and frequently exceeded expectations</p> <p>✓</p> <p>✓</p>
<p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05.</p>	
<p><b>Timeliness</b></p> <p>All outputs will be delivered to timeframes as agreed between the Minister and the Secretary to the Treasury for 2004/05.</p>	

Cost (\$000)

2004/05 Actual	3,382
Supp. Est - Voted	3,659
Main Est.	4,327
2003/04 Actual	3,507

(Figures are GST inclusive)

Actual 2004/05 output class expenditure was \$277,000 or 8% under Supplementary Estimates budgets owing largely to staff working on output class 9 outputs.

The appropriation for this output class was decreased by \$668,000 in the Supplementary Estimates owing to amalgamating two sections, which resulted in savings and lower accommodation project operating costs.

\* General service performance objectives are detailed on pages 71 to 72.

## Policy Advice: Tax

This class of outputs involves the provision of advice on tax policy and contributes to raising required tax revenue at least cost to the economy in line with fiscal strategy.

The Treasury, jointly with the Policy Advice Division of Inland Revenue, will provide advice on:

- tax strategy (overall objectives of the tax system, including choice of tax bases and the mix of taxation)
- international taxation (including taxation agreements with other countries; tax on New Zealanders' foreign-source income; and the taxation of income earned by New Zealanders overseas)
- personal taxation (that is, direct taxes imposed on individuals)
- indirect taxes (including GST and taxes on specific goods and services, like excises)
- corporate taxation (that is, direct taxes imposed on companies, trusts and other forms of legal entity; and taxes imposed on individuals through such business organisations)
- tax systems and compliance (including withholding taxes, tax penalties, taxation administration rules, taxpayer rights and obligations and taxpayer compliance costs).

The Government purchases tax policy advice from both the Treasury and Inland Revenue to ensure that its tax policies are based on all relevant economic, legal and administrative factors.

The Treasury will also provide advice, in cooperation with the collection agencies, on excises that are not collected by Inland Revenue.

In respect of Votes Revenue and Customs, the Treasury will provide:

- advice on the cost, quality and quantity of output sought by the Government, the financial performance of the departments, and the capability of the departments
- monitoring of payments for outputs against appropriations and advice on the non-departmental revenue and expenditure administered by the departments.

### Significant work completed during the year

- Advised on the taxation of financial intermediaries, including substantial consultation as part of Craig Stobo's *Towards Consensus on the Taxation of Investment Income* project and development of policy options contained within the Inland Revenue *Taxation of Investment Income* government discussion document.
- Advised on reforms to depreciation rates to ensure capital is used more efficiently.
- Provided advice on reforms to the taxation of new migrants to ensure that tax is not a disincentive to recruitment of migrants by New Zealand businesses.
- Advised on temporary exemption from tax on the capital gain for non-residents selling shares in certain venture capital investments in order to attract non-resident investment venture capital.
- Provided policy advice on the tax treatment of securities lending.
- Provided policy analysis on fast-growing companies.
- Advised on indexation of personal income tax thresholds.

- Advised on the taxation of banks, with the result that a thin capitalisation approach has now been enacted.
- Reformed the tax treatment of income from Australian superannuation schemes to address a significant impediment to a seamless trans-Tasman labour market.
- Updated a strategy for Double Tax Agreement (DTA) negotiations: applying this strategy to individual countries including the DTA with Poland and Protocol to the DTA with Australia.
- Advised on development of gas exploration incentives.

Service performance\*

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <ul style="list-style-type: none"> <li>• All reports will comply with the Quality Standards for Analysis and Advice. The Minister will be requested quarterly to indicate his level of satisfaction with the overall quality of outputs.</li> <li>• Outputs produced under this output class are to be undertaken in conjunction with Inland Revenue and other relevant collection agencies where reports are produced on revenue policy issues.</li> </ul>	<p>Met and frequently exceeded expectations</p> <p>✓</p>
<p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05.</p>	<p>✓</p>
<p><b>Timeliness</b></p> <p>All outputs will be delivered to timeframes as agreed between the Minister and the Secretary to the Treasury for 2004/05.</p>	<p>✓</p>

Cost (\$'000)

2004/05 Actual	2,670
Supp. Est - Voted	2,696
Main Est.	2,767
2003/04 Actual	1,859

(Figures are GST inclusive)

Actual 2004/05 output class expenditure was \$26,000 or 1% under Supplementary Estimates budgets. The appropriation for this output class was decreased by \$71,000 in the Supplementary Estimates.

\* General service performance objectives are detailed on pages 71 to 72.

## Budget Management

This class of outputs covers the development of Budget strategy, and the management and delivery of the Budget process. These outputs contribute to an efficient, effective and innovative State sector by providing credible public sector management and decision-making systems that encourage value for money.

In addition to managing the annual Budget, outputs include the provision of advice to identify and implement further improvements in the design of the Budget process. The focus is on:

- supporting and implementing amendments to the Public Finance and Fiscal Responsibility Acts
- improving value for money, including better use of evaluation.

### Significant work completed during the year

- Provided advice to the Government on spending pressures and priorities to assist in developing its strategy for the 2005 Budget.
- Managed the 2005 Budget round.
- Managed appropriation and Imprest Supply Bills, Estimates and Baseline Updates.
- Prepared the Public Finance (State Sector Management) Bill for introduction and recommended amendments. Also supported select committee consideration of the Bill.
- Identified possible options for promoting performance through the Budget system.

### Service performance\*

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <ul style="list-style-type: none"> <li>• All reports will comply with the Quality Standards for Analysis and Advice. The Minister will be requested quarterly to indicate his level of satisfaction with the overall quality of outputs.</li> <li>• Outputs produced under this output class: <ul style="list-style-type: none"> <li>- will meet the agreed standard for publication of parliamentary papers</li> <li>- will be prepared within the Budget timetable set by the Government and the statutory time limits of the Public Finance Act 1989.</li> </ul> </li> </ul>	<p>Met and frequently exceeded expectations</p> <p>✓</p> <p>✓</p>
<p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05.</p>	<p>✓</p>
<p><b>Timeliness</b></p> <p>All outputs will be delivered to timeframes as agreed between the Minister and the Secretary to the Treasury for 2004/05.</p>	<p>✓</p>

## Cost (\$'000)

2004/05 Actual	2,763
Supp. Est - Voted	2,774
Main Est.	2,338
2003/04 Actual	2,241

(Figures are GST inclusive)

Actual 2004/05 output class expenditure was \$11,000 or 0.4% under Supplementary Estimates budgets.

The appropriation for this output class was increased by \$436,000 in the Supplementary Estimates owing largely to increased resources required to implement changes to the Public Finance Act and Budget design work, which were partly offset by lower accommodation project operating costs.

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\* General service performance objectives are detailed on pages 71 to 72.

## Economic and Fiscal Forecasting and Reporting

This class of outputs involves the preparation of macroeconomic and fiscal forecasts, and the monitoring of economic and fiscal conditions.

Economic and fiscal updates are published in the middle of the financial year (typically in December) and at the time of the Budget (typically in May). Monitoring outputs include reports on major economic data releases and preparation of the annual and monthly financial statements of the Crown. In addition, the Minister is provided with regular assessments of how current events are affecting the economic and fiscal outlooks since the last update as an aid to Budget decision-making.

The output class also includes advice on the application and development of GAAP as it applies to the Crown. It also includes assessments of the adequacy of departmental management controls to detect or prevent errors in the financial information submitted to the Treasury.

These outputs contribute to the understanding by Ministers, Parliament and the public of the expected and actual consequences of government decisions, by entity and in the aggregate.

### Significant work completed during the year

- Prepared and published the annual financial statements for the year ended 30 June 2004 and the monthly financial statements for the Crown, the *December 2004 Economic and Fiscal Update* and the *2005 Budget Economic and Fiscal Update*.
- Reported and advised on developments in the domestic economy and the implications for the macroeconomic forecasts through commentary on key statistical releases and providing monthly summaries of key economic indicators.
- Provided advice on accounting policy issues including foreshore and seabed, Kyoto climate change obligations, and harmonisation of GAAP to Government Financial Statistics and System of National Accounts (SNA) frameworks.
- Provided advice and representation in relation to public sector accounting standard-setting issues. This included the conversion of New Zealand's financial reporting standards to the international standards, representation on Accounting Standards Review Board meetings and preparation of submissions to FRSB on financial reporting exposure drafts to develop financial reporting from a public-sector perspective.
- Obtained a comprehensive re-assessment of the quality of financial internal controls in government departments (the Departmental Internal Control Evaluation process).
- Established process, specifications and guidance for the Public Finance Amendment Act 2004 implementation, and implemented mandatory elements for Budget 2005.

Service performance\*

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <ul style="list-style-type: none"> <li>All reports will comply with the Quality Standards for Analysis and Advice. The Minister will be requested to indicate his level of satisfaction with the overall quality of outputs.</li> <li>Forecasting publications produced under this output class will meet the requirements of the Fiscal Responsibility Act 1994.</li> <li>The Crown financial statements will conform with GAAP and fairly reflect the operations, cash flows and financial position of the Crown for the year ending 30 June 2004, the quarter ending 30 September 2004, and at monthly intervals after that until the end of the financial year.</li> <li>The daily Controller function will monitor accurately the year-to-date disbursements compared with the supply made available by Parliament, and a Controller statement will be prepared for the Controller and Auditor-General's signature authorising the release of public money.</li> <li>Delegations for the management of foreign-exchange risks, Crown bank accounts and trust money will be managed to ensure that the conditions of the delegations are not breached and that they permit financial activity to be authorised at an appropriate level.</li> <li>Management statements required under section 29 of the Public Finance Act 1989 will be signed within the time limits set out in that Act and will be supported by analysis and reviews of departmental financial management.</li> </ul>	<p>Met and frequently exceeded expectations</p> <p>✓</p> <p>✓</p> <p>✓</p> <p>✓</p> <p>✓</p> <p>✓</p>
<p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05.</p>	<p>✓</p>
<p><b>Timeliness</b></p> <p>All outputs will be delivered to timeframes as agreed between the Minister and the Secretary to the Treasury for 2004/05.</p>	<p>✓</p>

Cost (\$000)

2004/05 Actual	6,809
Supp. Est - Voted	7,014
Main Est.	6,303
2003/04 Actual	6,914

(Figures are GST inclusive)

Actual 2004/05 output class expenditure was \$205,000 or 3% under Supplementary Estimates budgets.

The appropriation for this output class was increased by \$711,000 in the Supplementary Estimates owing largely to additional resources required to implement changes to the Public Finance Act and work on implementing New Zealand international accounting standards in the public sector. These increases were partly offset by lower accommodation project operating costs.

\* General service performance objectives are detailed on pages 71 to 72.

## Debt and Related Financial Asset Management

Outputs in this class contribute to achieving an optimal Crown balance sheet and concern the operational management of the Crown's portfolio of sovereign-issued debt and associated financial assets. All expenses for this output class are incurred under section 61 of the Public Finance Act 1989. Specific activities include:

- developing and maintaining an appropriate framework for efficiently managing the portfolio and the risks associated with it
- issuing domestic-currency debt to meet the Government's funding requirements
- disbursing cash to departments and facilitating departmental cash management
- advancing funds to government entities in accordance with Government policy
- providing capital market services and derivative transactions for departments and government entities
- funding the Reserve Bank's foreign-exchange reserves
- managing foreign-currency assets required to meet net foreign-currency interest and principal payments
- maintaining hedges of foreign-currency debt that cannot be bought back from investors
- adding value to the Crown in undertaking activities whilst conforming to a risk-averse management framework
- maintaining a diversified funding base and, where appropriate, enhancing relationships with investors who hold, or are potential holders of, New Zealand government securities and with financial intermediaries and the international credit rating agencies
- developing and maintaining an appropriate infrastructure of systems, monitoring, accounting and reporting for the portfolio.

### Significant work completed during the year

- Issued \$2,150 million of Government bonds to meet the Government's funding requirements.
- Completed \$1,150 million of interest-rate swaps under the domestic swap programme.
- Completed \$22 billion of foreign currency transactions (including foreign-currency swaps) for the NZSF.
- Provided US\$623 million and EUR 140 million in loans, and issued \$1 billion of bonds as a capital injection, to the Reserve Bank of New Zealand (RBNZ) under new funding arrangements to support the Bank's foreign-currency intervention capability.
- Executed a new two-year pricing agreement with the Guardians of the NZSF to hedge their foreign-currency exposures in up to 13 currencies.
- Concluded the re-negotiation of the Crown's transactional banking contract with Westpac, executed the domestic transaction banking services Master Agreement, and secured a three-year fixed-pricing arrangement for these banking services.
- Completed the transition of registry services provision from RBNZ to Computershare Investor Services.

- Provided advice on the implementation and administration of immigration bonds as a component of revisions to the immigration investor category announced in June 2005.
- Continued work on the accounting implications for the NZDMO and Crown financial reporting of changes to international financial accounting and reporting standards.
- Continued to develop proposals for infrastructure bonds to fund transport investments, including borrowing by Transit New Zealand to support the ALPURT B2 toll road, Auckland’s northern motorway extension.

Service performance\*

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <ul style="list-style-type: none"> <li>• All reports will comply with the Quality Standards for Analysis and Advice. The Minister will be requested quarterly to indicate his level of satisfaction with the overall quality of outputs.</li> <li>• The Secretary to the Treasury will monitor the operation of NZDMO with the assistance of an Advisory Board. Performance in portfolio management, debt issuance, capital market transactions and advice, transactional processing, and compliance with risk management policies will be reported regularly to the Secretary to the Treasury and the Advisory Board, and to the Minister in the context of the Treasury’s quarterly and year-end reviews.</li> <li>• Policies regarding the strategic objectives for domestic- and foreign-currency debt, instruments and currencies for transactions, limits in respect of market and credit risk utilisation, composition requirements for the liquidity asset portfolio, and maturity profile requirements will be adhered to.</li> <li>• Policies, delegations, limits, reporting and performance management requirements, procedural manuals, and established processes, and other controls for managing internal operations will be adhered to.</li> <li>• Issuance of domestic-currency debt will be transparent and predictable.</li> </ul> <p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05.</p> <p><b>Timeliness</b></p> <p>All outputs will be delivered to timeframes as agreed between the Minister and the Secretary to the Treasury for 2004/05.</p>	<p>Met and frequently exceeded expectations</p> <p>✓</p> <p>✓</p> <p>✓</p> <p>✓</p> <p>✓</p> <p>✓</p>

Cost (\$000)

2004/05 Actual	4,745
Supp. Est - Voted	4,969
Main Est.	5,623
2003/04 Actual	5,274

(Figures are GST inclusive)

Actual 2004/05 output class expenditure was \$224,000 or 5% under Supplementary Estimates budgets owing largely to staff vacancies and lower operating costs.

The appropriation for this output class was decreased by \$654,000 in the Supplementary Estimates owing largely to staff vacancies, lower operating costs and lower accommodation project operating costs.

\* General service performance objectives are detailed on pages 71 to 72.

## Management of Claims Against the Crown, Contractual Liabilities and Crown Properties

This output class involves managing a range of commercial, contractual and Treaty of Waitangi-related claims against the Crown. Outputs in this class contribute to minimising Crown financial risk within the bounds of Government objectives. Specific outputs within this class include:

- management of commercial and contractual risks associated with the 1973 Maui gas contracts, including the operation of the gas notification system with downstream gas users
- management of contractual and commercial issues arising from completed asset sales and wind-up of the Crown's previous ownership interests in SOEs, Crown companies and other entities
- advice on the management of historical claims under the Treaty of Waitangi and assistance with the Crown's negotiation of specific settlements
- provision of legal title to land sold to SOEs and other Crown companies as a part of their sale and purchase agreements with the Crown
- management of former Ministry of Foreign Affairs and Trade (MFAT) overseas properties that have been transferred to the Crown
- management of the export credit guarantee policy and scheme.

Specific outputs in this class often depend on the actions of third parties.

### Significant work completed during the year

- Implemented the new contractual arrangements arising out of the re-negotiations of the Maui gas contracts, and ongoing discussions on open access to the Maui pipeline.
- Substantially completed negotiations to transfer the Crown's geothermal interests to Mighty River Power.
- Completed disposal of the Crown's interests in Tarawera Forests Ltd.
- Provided advice on specific historical Treaty of Waitangi settlement negotiations, and on wider policy settings.
- Continued the programme of identifying and transferring legal land title to various SOEs and other companies.
- Provided ongoing management of the Export Credit Office (ECO) operations, with maintained emphasis on communications and marketing which contributed to the completion of three deals.
- Managed a portfolio of properties occupied by MFAT, including routine refurbishment projects and investigating options to refurbish New Zealand House in London and accommodate New Zealand's diplomatic presence in the United Kingdom over the medium term.

Service performance\*

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <p>All reports will comply with the Quality Standards for Analysis and Advice. The Minister will be requested quarterly to indicate his level of satisfaction with the overall quality of outputs.</p> <ul style="list-style-type: none"> <li>• Outputs produced under this output class will:                             <ul style="list-style-type: none"> <li>- explore all opportunities to reach a satisfactory settlement of liabilities within parameters set by Ministers ✓</li> <li>- meet the Treasury’s policies and procedures for the employment of advisors and consultants ✓</li> <li>- meet the Crown’s contractual responsibilities and enforce the Crown’s contractual rights. ✓</li> </ul> </li> <li>• The Secretary to the Treasury will monitor the operation of the ECO with the assistance of an Advisory Board. It is expected that performance will conform with international best practices for the provision of export credit insurance. ✓</li> </ul>	Met and frequently exceeded expectations
<p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05. ✓</p>	
<p><b>Timeliness</b></p> <p>All outputs will be delivered to timeframes as agreed between the Minister and the Secretary to the Treasury for 2004/05. ✓</p>	

Cost (\$000)

2004/05 Actual	2,582
Supp. Est - Voted	2,872
Main Est.	4,147
2003/04 Actual	4,163

(Figures are GST inclusive)

Actual 2004/05 output class expenditure was \$290,000 or 10% under Supplementary Estimates budgets. This variance was mainly owing to Maui gas court costs being awarded to the Crown, ECO review being deferred, reduced demand for New Zealand House outputs and Maui gas costs being less than forecast.

The appropriation for this output class was decreased by \$1.275 million in the Supplementary Estimates owing largely to lower demand for Maui gas outputs and lower accommodation project operating costs.

\* General service performance objectives are detailed on pages 71 to 72.

## Policy Advice: Ownership and Performance of Crown Companies and Financial Institutions

This output class involves the provision of policy advice on the Crown's financial position and the Crown's ownership interest in Air New Zealand, Crown companies (including SOEs) and CFIs. This contributes towards enhancing and protecting the value of the Crown's interest in these institutions.

The outputs in this class include:

- advice to the Minister of Finance, as shareholder in SOEs, CRIs and other Crown companies, on issues impacting on the Crown's ownership strategies, business plans and SOIs, capital structure, dividends, diversification and expansion proposals, and divestments. This also includes advice on Air New Zealand, rail infrastructure and other entities where the Crown has an ownership interest
- advice on significant company restructurings, and on establishing commercially related activities in an appropriate institutional form and on Crown negotiations in relation to changes in asset structure and form
- advice on the Crown's ownership interests and guarantee and indemnity obligations in relation to the Government Superannuation Fund, the National Provident Fund, Public Trust, the Earthquake Commission and the NZSF, especially in relation to Crown financing, financial performance, management of risk (as owner or guarantor), unfunded Crown liabilities, and any residual implementation issues in relation to the NZSF.

### Significant work completed during the year

- Concluded four strategic ("long-term hold") reviews and progressed three other reviews.
- Provided shareholding Ministers with advice on SOE and Crown company business plans and statements of corporate intent, and on a range of specific company issues.
- Provided advice to Ministers on the expansion of New Zealand Railways Corporation (NZRC) role as it became the track operator, and other rail-related issues.
- Provided advice on CFI performance, including investment returns, appointments, statements of intent, and on a range of specific issues.
- Managed the process for an independent review of the operation of the NZSF.

Service performance\*

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <p>All reports will comply with the Quality Standards for Analysis and Advice. The Minister will be requested quarterly to indicate his level of satisfaction with the overall quality of outputs.</p> <ul style="list-style-type: none"> <li>• Outputs produced under this output class will be undertaken in conjunction with CCMAU where reports are prepared on the financial performance of SOEs, CRIs and other Crown companies and in conjunction with the Ministry of Housing in relation to Housing New Zealand Corporation.</li> </ul>	<p>Met and frequently exceeded expectations</p> <p>✓</p>
<p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05.</p>	<p>✓</p>
<p><b>Timeliness</b></p> <p>All outputs will be delivered to timeframes as agreed between the Minister and the Secretary to the Treasury for 2004/05.</p>	<p>✓</p>

Cost (\$000)

2004/05 Actual	3,007
Supp. Est - Voted	3,070
Main Est.	3,292
2003/04 Actual	2,904

(Figures are GST inclusive)

Actual 2004/05 output class expenditure was \$63,000 or 2% under Supplementary Estimates budgets.

The appropriation for this output class was decreased by \$222,000 in the Supplementary Estimates owing largely to consulting work costing less than forecast and lower accommodation project operating costs.

\* General service performance objectives are detailed on pages 71 to 72.

## Policy Advice: Regulation and Vote Purchase, Ownership and Performance Issues

This class of outputs contributes primarily to ensuring that the State's resources and regulatory powers are used effectively and efficiently to achieve the Government's desired outcomes, including a stable and sustainable macroeconomic environment.

The outputs include:

- advice on cost, quality and quantity of output sought by the Government, the financial performance of departments and Crown entities, and the capability of departments and Crown entities
- monitoring of appropriations to ensure expenditure is within parliamentary authority and advice on the non-departmental revenue and expenditure administered by departments and Crown entities
- identification and assessment of opportunities for the Government to achieve its goals relating to improving economic performance, inclusive society, environmental management and an efficient and effective State sector.

Areas covered are:

- health
- education
- welfare (including housing and social services)
- justice
- labour market (including employment, immigration and ACC)
- population agencies
- external linkages, defence and national security
- research, science and technology
- economic development (regional and industry development and firm performance)
- the regulatory environment (for example business law and competition policy)
- infrastructure (including energy, telecommunications, water and transport)
- environment
- primary sector
- government services (for example Internal Affairs, SSC, local government)
- parliamentary agencies.

### Significant work completed during the year

- Developed and reviewed health sector productivity trends, with an emphasis on options to improve productivity over time.
- Reported to the Minister of Finance on the scope of the proposed medium-term review of health expenditure and the implications for the evolution of health funding beyond the 2006/07 fiscal year.
- Worked on developing benchmarking methodologies to measure District Health Board technical efficiency.
- Participated in the Ministry of Health Working Group on System Performance and Assessment.
- Provided advice and worked with the Ministry of Health on addressing short- and long-term policy and funding issues, in relation to the health of older people and disability support services.
- Participated in the Working Party on Support Services for Older People and People with Disabilities.
- Provided advice on Early Childhood Education regulatory policies and funding rates, teachers' pay negotiations and school property issues.
- Provided advice on tertiary funding issues including proposed changes to sub-degree funding arrangements and on long-term funding issues.
- Provided advice on student debt, student support package and tertiary pre-savings, school funding issues and several school sector business cases.
- Contributed to the review of the application of generic Crown entity legislation to Tertiary Education Institutions.
- Provided advice on specific Tertiary Education Institution ownership risks and the New Zealand Qualifications Authority's budget and fees.
- Provided advice on the fit of the education Budget initiatives with the size and structure of the Education Budget Allocation and the completion and documentation of the education Budget package.
- Jointly led a central agency review of machinery of government issues and the education sector agencies.
- Provided advice on the development of a work-based savings scheme.
- Provided advice on possible approaches to government interventions to assist low-income families into first home ownership as part of an interdepartmental Home Ownership Steering Committee, culminating in the home ownership interventions forming part of the Budget 2005 Kiwisaver package.
- Provided advice on options for a tertiary education savings scheme, managed requests for expressions of interest and provided advice on the response from the savings sector.
- Wrote a background paper for the Hui Taumata on Māori economic development.
- Assisted the Workplace Productivity Working Group to complete its report, *The Workplace Productivity Challenge* released in November 2004.
- Published four Treasury Working Papers on human capital and growth.

- Undertook a major project on labour force participation, reviewing the facts and context of New Zealand's past, current and prospective future performance, which culminated in a workshop and working papers. This work provided the basis for advice to Ministers on the development of the Government's policies on labour force participation, as well as providing input for the OECD's annual economic survey of New Zealand.
- Began work on measuring productivity in the public sector, to improve the Treasury's ability to assist departments when designing regimes for determining the most appropriate level of publicly provided goods and services.
- Contributed to departmental advice on various initiatives (including the use of immigration) to address skill and labour shortages, including the development of a medium-term skills and labour force strategy and the extension of the Government's industry partnerships.
- Undertook research on the way the labour market is adjusting to current and predicted skill and labour shortages.
- Contributed to the design of the single core benefit framework, with a focus on how the framework could be used to increase work incentives.
- Provided advice on the work incentives faced by secondary earners and potential options for changing these incentives.
- Worked with the Department of Labour and MSD to provide advice on the restructuring of community employment activities.
- Worked with the Department of Labour on capability- and strategy-related issues arising from its repositioning exercise.
- Reported (with MED and RBNZ) on regulation of major financial institutions.
- Participated in establishing the Trans-Tasman Council on Banking Supervision.
- Advised the Minister and Cabinet on progress in moving towards a single economic market with Australia and identifying potential priorities.
- Provided policy input for China FTA negotiations, Thailand FTA negotiations, ASEAN-Australia/New Zealand FTA negotiations, and P3 CEP negotiations.
- Provided advice on pressures on the National Land Transport Fund and options to accelerate land transport projects.
- Provided advice on the ALPURT B2 toll project, Auckland's northern motorway extension.
- Provided advice on the Western Corridor Transportation Study and further funding for the Wellington Western Corridor.
- Provided advice on marginal pricing in electricity markets.
- Provided advice on regulation of gas pipeline access.
- Investigated the sustainability of local government funding.
- Provided advice, with other officials, on changes to Resource Management Act legislation and associated instruments, including proposed national policy statements.
- Provided advice, with other officials, on approaches for managing freshwater resources.
- Provided advice on land policy issues including public access to land, Public Works and Land Act reviews and possible approaches to high country tenure review.

- Provided advice on the emissions charge, New Zealand's revised net emissions position under the Kyoto Protocol and on valuing the associated liability, for recognition in the Crown Financial Statements.
- Provided advice to the Ministry for the Environment on Negotiated Greenhouse Agreements.
- Provided advice on managing biosecurity risks, the foot and mouth hoax, painted apple moth, fall web worm, didymosphenia geminata and southern salt marsh mosquito incursions.
- Provided advice to Ministers on access to finance and the creation of the Seed Co-investment Fund.
- Provided advice on a process to establish a new Department of Building and Housing.
- Provided advice on initial and interim findings of the work to identify Long Term Capital Requirements of Housing New Zealand Corporation (HNZC), including operationalising the Modernisation Policy Statement.
- Provided advice on enhancing the weather-tight homes disputes resolution process and modelling fiscal implications of assisting home owners to undertake repairs to homes while liability issues are being resolved.
- Reported on the expansion of Auckland Regional Women's Corrections Facility; worked with the Department of Corrections on managing additional inmates in both the short and medium term; and on capital expenditure risks, particularly at Mt Eden and Springhill.
- Worked with Justice Sector agencies on managing the Justice Sector contingency in 2004/05, particularly the likely increases in Vote Corrections.
- Contributed to and provided advice on the Ministry of Justice Baseline Review implementation.
- Provided advice on the Department of Child, Youth and Family Services' Non-Departmental Output Class Review including: the progress of an early intervention package, which included proposals to enhance CYF's management information.
- Participated in the Defence Capability and Resourcing Review and the Defence Funding Package and advice to Government on defence capital acquisitions.
- Contributed to advice on the future use of Whenuapai Airbase.

## Service performance\*

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <p>All reports will comply with the Quality Standards for Analysis and Advice. The Minister will be requested to indicate his level of satisfaction with the overall quality of outputs.</p>	Met and frequently exceeded expectations
<p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05.</p>	✓ <sup>1</sup>
<p><b>Timeliness</b></p> <p>All outputs will be delivered to timeframes as agreed between the Minister and the Secretary to the Treasury for 2004/05.</p>	✓

### Cost (\$000)

2004/05 Actual	24,328
Supp. Est - Voted	24,575
Main Est.	23,159
2003/04 Actual	25,363

(Figures are GST inclusive)

Actual 2004/05 output class expenditure was \$247,000 or 1% under Supplementary Estimates budgets.

The appropriation for this output class was increased by \$1.416 million in the Supplementary Estimates owing largely to increased demand for a range of outputs in this output class. These increases were partly offset by lower accommodation project operating costs.

\* General service performance objectives are detailed on pages 71 to 72.

- 1 Some deadlines were extended, with the agreement of the Minister, because of:
- higher-priority work
  - legislative delays
  - the need for more analysis and/or consultation than originally envisaged.

## Service Performance Objectives: All Vote Finance Output Classes

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <p>All reports will comply with the Quality Standards for Analysis and Advice outlined on page 133. Output quality will be assessed as follows:</p> <ul style="list-style-type: none"> <li>The Minister will expect the Treasury to implement suitable quality control procedures to support the expectations for analysis and advice delivered under this Vote.</li> <li>Managerial and peer (internal and external) review will be maintained to ensure that the quality standards are met.</li> <li>The Minister will be formally requested, on a quarterly basis, to indicate his level of satisfaction with the overall quality of the outputs produced.</li> </ul>	<p>✓</p> <p>✓</p> <p>Met and frequently exceeded expectations</p>
<p><b>Coverage</b></p> <p>A comprehensive range of services will be provided as agreed with the Minister. These will include the capacity to react quickly and provide support for the Minister in Cabinet committees, including relevant briefings on significant issues and regular evaluation of the impacts of policy on the Government’s desired outcomes.</p>	<p>✓</p>
<p><b>Cost Effectiveness</b></p> <p>Analysis and advice will be delivered within the cost parameters agreed with the Minister (or as subsequently modified by agreement).</p>	<p>✓</p>
<p><b>Timeliness</b></p> <p>Timeframes will be agreed between the Minister and the Secretary to the Treasury for the financial year.</p> <ul style="list-style-type: none"> <li>Advice will be delivered within the agreed and/or statutory timeframe so that Ministers have sufficient time to consider the issues and take appropriate action. Where agreed deadlines will not be met, extensions are to be formally requested.</li> <li>Ministerial correspondence (MCs), parliamentary questions (PQs), Cabinet agendas and Official Information Act requests (OIAs) will be responded to within agreed and/or statutory timeframes.</li> <li>The Department will respond appropriately to requests for attendance at Parliament during debates and at Cabinet and select committee meetings.</li> <li>Drafting instructions in the form of draft legislation will be provided to the Parliamentary Counsel Office within the timeframe agreed with that Office.</li> <li>Quarterly and end-of-year reporting will enable the Minister to assess actual performance in the timeliness of output delivery against those expectations.</li> </ul>	<p>✓</p> <p>Refer page 72</p> <p>✓</p> <p>✓</p> <p>✓</p>

2004/05	PQs	MCs	OIAs
<b>Policy Advice: General Economic &amp; Fiscal Strategies</b>			
Estimated	10-20	80-120	10-20
Actual draft replies	6	86	5
% answered by due date	100	93	60
<b>Policy Advice: Financial &amp; Public Sector Management Systems</b>			
Estimated	0-5	10-20	0-5
Actual draft replies	-	3	-
% answered by due date	-	100	-
<b>Policy Advice: Tax</b>			
Estimated	10-20	100-150	10-20
Actual draft replies	4	308	16
% answered by due date	100	79	94
<b>Budget Management</b>			
Estimated	10-20	10-20	5-20
Actual draft replies	3	-	3
% answered by due date	100	-	100
<b>Economic &amp; Fiscal Forecasting &amp; Reporting</b>			
Estimated	50-60	0-5	0-5
Actual draft replies	147	11	7
% answered by due date	99	100	100
<b>Debt &amp; Related Financial Asset Management</b>			
Estimated	0-5	0-5	-
Actual draft replies	7	1	1
% answered by due date	100	100	100
<b>Management of Claims Against the Crown, Contractual Liabilities &amp; Crown Properties</b>			
Estimated	5-10	5-10	0-5
Actual draft replies	-	4	6
% answered by due date	-	100	83
<b>Policy Advice: Ownership &amp; Performance of Crown Companies &amp; Financial Institutions</b>			
Estimated	15-30	130-180	25-45
Actual draft replies	13	66	24
% answered by due date	100	100	96
<b>Policy Advice: Regulation &amp; Vote Purchase, Ownership &amp; Performance Issues</b>			
Estimated	150-200	200-325	150-200
Actual draft replies	202	598	67
% answered by due date	95	87	90
<b>Ownership</b>			
Estimated	10-20	0-5	0-5
Actual draft replies	41	2	4
% answered by due date	100	100	100

## Explanation:

- All PQs were provided to the Clerk's office by the due date, but a few failed to meet our internal deadline to the Minister's office, typically by one day.
- Most of the late MCs and OIAs were provided one day after our internal deadline.
- The balance of MCs and OIAs tended to be late because they involved complex or multiple issues and/or required additional information or agreement from third parties. This was exacerbated by staff absences over holiday periods and workload pressures, particularly for small teams.

# CCMAU

## – VISION AND PURPOSE

### Vision

The New Zealand Government's ownership advisor of choice in the provision of commercial advice – a sought-after leader, highly respected worldwide for what we do.

### Purpose

CCMAU contributes to the efficient management of the Crown's assets and liabilities by providing services which enable shareholding Ministers to hold Crown company and entity boards accountable for their performance in maintaining and enhancing shareholder value.

CCMAU monitors companies and entities to advise Ministers on: company and entity performance; significant investment and divestment decisions by boards; and strategies to achieve effective management of the Crown's assets.

CCMAU provides services in the following areas:

- Monitoring – reporting on business plans, company reports, performance against targets and sectoral trends.
- Ownership advice – advising on strategic issues, investment and diversification opportunities, restructuring issues, and the impact of policy positions.
- Ministerial servicing – managing issues and drafting replies to correspondence, PQs and OIAs.
- Governance – identifying and screening potential directors, managing the appointments' processes and promoting best-practice corporate governance of Crown companies and entities.

### Relationship with the Treasury

The Executive Director of CCMAU is directly accountable to the Secretary to the Treasury for the Crown's investment in CCMAU, and for CCMAU's performance in providing the output classes Ministers seek.

## CCMAU EXECUTIVE SUMMARY



Executive Director – Murray Wright

CCMAU aims to be the Government's ownership advisor of choice in the provision of commercial advice on a portfolio of companies and entities owned by the Crown. This year, we have continued the sectoral focus to our work and have taken an active role in assisting Ministers to clarify their ownership expectations for many of the companies and entities in our portfolio.

During 2004/05, CCMAU has continued to focus on providing timely, high-quality commercial advice to shareholding Ministers. We have continued to refine the way we do things so that our outputs make a difference to our stakeholders and have actively built strong relationships across the public sector.

We have maintained our focus on implementing the Government's long-term ownership policy – to date, owner's reviews have been completed for six SOEs and another three reviews are in progress. Also, the CRI Operating Framework was refined and company-specific addenda were added for the first time. Our Appointments and Governance team was actively involved in a significant number of director appointments and reappointments during the year that included five changes of Chair.

Our attention to addressing a number of issues that would help make CCMAU a better place to work has had a very positive effect. We have a talented team of individuals across all sector groups and CCMAU is strongly placed to meet Ministers' ongoing expectations.

### Science and innovation sector

#### Sector Manager – Adrian Wimmers

The Crown-owned science and innovation companies (nine CRIs and the New Zealand Venture Investment Fund Ltd (VIF)) continue to make significant contributions to two of the Government's cornerstone strategies – the Growth and Innovation Framework (GIF) and Sustainable Development.

Through these strategies, the Government aims to move New Zealand towards an economy based on sustainable innovation. Scientific research, and the transfer of technologies developed through such research, has a pivotal and increasing role in achieving this goal.

The Government has established clear expectations for the CRIs and VIF. During 2004/05, CCMAU worked with the Minister for CRIs, and in consultation with MoRST and the Treasury, to refine the CRI Operating Framework and, in particular, provide clearer expectations regarding the interface between commercial activities and working for the benefit of New Zealand. For the first time, the Operating Framework included company-specific addenda that provided greater clarification to individual boards on particular matters relevant to their CRI.

CCMAU and the Treasury supported MoRST's efforts to establish Research and Education Advanced Network New Zealand Ltd (REANNZ). REANNZ will establish and operate an advanced network to promote education, research and innovation for the benefit of New Zealand. CCMAU will assume monitoring responsibility for REANNZ following its incorporation.

During the year, CCMAU continued to develop its relationships and visibility across the innovation sector, with the aim of being better able to advise shareholding Ministers and contribute to and/or lead the development of relevant policy. Our involvement in establishing the Ocean Survey 20/20 programme, securing support for a National Centre for Biosecurity and Infectious Disease, and reviewing the future viability of the National Isotope Centre were all examples of our increased level of cross-departmental working. In 2005/06, we intend to enhance further our relationships with other organisations in the sector.

Our role in the Equity Investment Fund (EIF) continued, notably through our work in the due diligence process for a \$5 million investment in one CRI. We expect demand for EIF funds to increase in coming years, as CRI commercialisation activities lead to capital constraints.

## Energy, land and environment sector

### Sector Manager – Michael Moore

The Energy, Land and Environment (ELE) team advises the Minister for SOEs on the performance of, and issues relating to, the 13 SOEs that comprise the energy, land and environment sectors.

The energy sector companies control over \$9 billion in assets and have annual revenues of over \$3 billion, while land and environment sector companies control around \$1 billion in assets and have annual revenues of around \$335 million. These companies range from large electricity generator/retailers such as Meridian Energy Ltd (Meridian), Mighty River Power Ltd (Mighty River Power) and Genesis Power Ltd (Genesis) in the energy sector to a diverse range of companies in the land and environment sector such as AgriQuality Ltd (AgriQuality), Landcorp Farming Ltd (Landcorp), Quotable Value Ltd (Quotable Value) and Timberlands

West Coast Ltd (Timberlands West Coast). Collectively, ELE companies have a significant impact on the New Zealand economy.

Over the course of 2004/05, the energy sector continued to provide challenges, with a continuing need for investment in New Zealand's energy infrastructure in both energy production and distribution. The ELE team worked closely with energy sector SOEs as they developed plans to help build the nation's energy infrastructure, while meeting shareholder expectations over strategic direction and performance, both financial and non-financial.

We were also closely involved with land and environment sector companies as they faced a range of issues in 2004/05. The issues in which we contributed included:

- Timberlands West Coast's development of strategic options
- Landcorp's proposed disposal of two farm properties in the greater Wellington region
- Meteorological Service of New Zealand Ltd's (MetService's) relationship with the National Institute of Water and Atmospheric Research Ltd (NIWA)
- the increasingly competitive environment facing AgriQuality and Asure New Zealand Ltd (Asure).

The ELE team continued its focus on implementing the Government's long-term hold ownership policy, which will ultimately involve owner's reviews of all SOEs. These reviews cover key ownership expectations including:

- company strategy and scope of business
- company performance and benchmarking
- capital management – investment strategy, capital structure and dividend policy.

In 2004/05, we worked with the Treasury in completing reviews of Landcorp, MetService, Meridian and Solid Energy New Zealand Limited (Solid Energy). We have commenced reviews of AgriQuality and Asure. We expect our work in these reviews not only to provide Crown company boards with a much clearer understanding of the owner's expectations, but also to provide us with a clearer framework for developing our ownership monitoring expertise in the future.

## Communications, services and infrastructure sector

### Sector Manager – James Cunningham

The Communications, Services and Infrastructure (CSI) sector comprises a diverse group of companies in the broadcasting, telecommunications, services and transport infrastructure fields, as well as two Crown entities (Public Trust and the New Zealand Lotteries Commission).

These businesses collectively control approximately \$4.5 billion in total assets (or approximately \$2.3 billion after netting off Kiwibank Ltd's (Kiwibank's) and Public Trust's liabilities from their assets to avoid distortion), play a key role in

providing products and services to New Zealanders, and operate in a commercial way to generate profits and increase shareholder value.

Over the last year, we have assessed and advised shareholding Ministers on a number of matters, including:

- Dunedin International Airport Ltd's \$23.7 million terminal redevelopment project
- the extension of Invercargill Airport Ltd's runway to allow for trans-Tasman flights
- New Zealand Post Ltd's (New Zealand Post's) future strategies for its Express and Logistics Group, culminating in its decision to enter into a joint venture with DHL Worldwide Express for the express and logistics part of New Zealand Post's business
- the business case for Kiwibank's expansion into the small business banking market
- various Cabinet papers relating to NZRC, which now trades as ONTRACK
- the establishment of a framework to enable the reinvestment of Television New Zealand Ltd's (TVNZ's) dividends where these exceed the cost of the capital the Crown has invested in the company
- residual issues arising in respect of Terralink Ltd, a company in liquidation
- an acquisition made in Australia by Transmission Holdings Ltd's (THL) Australian subsidiary company THL Australia (Proprietary) Ltd, which is complementary to its existing business and helps diversify its revenue streams.

The Government's long-term ownership policy for SOEs and Crown companies has increased our role in ensuring shareholder value is protected and enhanced over the medium to long term, while allowing for a prudent level of commercial risk-taking in developing new initiatives. During the year, the CSI team commenced the long-term hold review of Airways Corporation of New Zealand Ltd (Airways).

## Appointments and governance

### Appointments and Governance Manager – Steve Rich

The appointments and governance function is the responsibility of a small dedicated team within CCMAU. Our primary focus is on managing, on behalf of Ministers, the appointment process for the 36 company and entity boards monitored by CCMAU. In the period 1 July 2004 to 30 June 2005, we advised Ministers on 119 separate appointments and reappointments to boards of SOEs, CRIs and other Crown companies and entities. Once appointment processes were complete, a number of day-long, sector-specific induction workshops were held to assist new directors to assimilate into their roles.

At 30 June 2005 there were 217 directors across all the boards, 137 male and 80 female. Of the total, 83% were European and 14% were Māori.

Of particular significance during the year were changes in a number of Chair positions. In particular, long-serving Chairs Errol Millar (Airways), Barney Sundstrum (Asure), Dr Francis Small (Meridian), Rob Challinor (Mighty River Power) and Sir Colin Maiden (Transpower New Zealand Ltd (Transpower)) were replaced by Con Anastasiou (Airways), Dr Richard Janes (Asure), Wayne Boyd (Meridian), Carole Durbin (Mighty River Power) and David Gascoigne (Transpower) respectively.

To assist us in managing appointments, we run a variety of processes to identify appropriate candidates for ministerial consideration. Although it is tailing off slightly, there continues to be high interest from skilled candidates in serving on Crown company boards. In 2005 we received approximately 130 general expressions of interest from new candidates, in addition to approximately 350 applications or nominations for specific roles under consideration (the majority of the latter group were already registered on our database).

We continue to meet as many of these people as possible, and in 2004/05 we met approximately 80 of the new candidates as part of our general screening process. Where warranted, candidates identified through this process were invited to attend one of the three “prospective director” training seminars that we hosted for director candidates.

As part of specific appointment processes, we also conducted 71 due diligence interviews and checking processes for candidates short-listed by Ministers for board consideration.

During the year, CCMAU continued to be approached by other Crown and private agencies for nominations of candidates whose attributes appear to meet the skill needs of non-CCMAU-monitored entities. In addition to providing best-practice advice and assistance where requested, we recommended candidates in response to 40 specific requests from other agencies.

The first biannual review of directors’ fees was completed in the 2004/05 year, but not in time to be considered before pre-election conventions stepped in. The results of the review are now scheduled to be considered by Cabinet in October 2005, with any changes implemented on 1 January 2006.

Ministers’ expectations that all boards complete annual evaluation processes are widely understood by boards. Towards the end of the year we commissioned a review of the board evaluation process and associated minimum requirements of boards. Any recommendations for change will be considered by Ministers later in 2005.

The Appointments and Governance team continues to be involved in the forum of governance officials that was convened as a networking and information-sharing exercise. CCMAU is represented on the forum Steering Committee and its various working-level groups. An area of focus for all agencies involved in the appointment process is the implementation of the Crown Entities Act 2004 which, amongst other things, has made a number of changes to the appointment process requirements that Ministers (and therefore officials) must follow.

## Maintaining and developing capability

### Setting strategic direction

During the year we further refined our strategic direction in response to our stakeholders' changing needs. We aim to achieve our vision by focusing on five organisational goals around leadership, product quality, capability, workplace and visibility. A number of initiatives are planned in 2005/06 to give effect to achieving these organisational goals.

We have continued to pay close attention to the quality and content of our outputs during 2004/05 with positive effect – our early involvement in a number of cross-sector policy-related issues demonstrates that.

Our advice has a commercial focus that encompasses both financial and non-financial performance, but is tempered by the range of shareholder expectations for the different groups of companies and entities we monitor.

### Managing our people

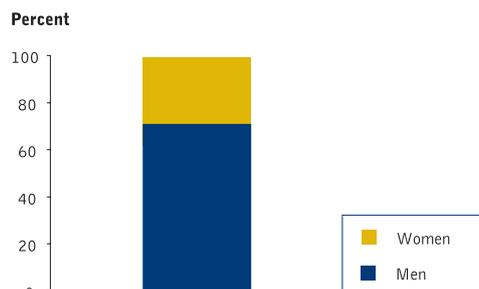
During the year we paid particular attention to addressing a number of issues that would help make CCMAU a better place to work. Some of the initiatives included upgrading our IT system, introducing a new records and document management system, continuing our commitment to staff training and development, and refining our staff policies to reflect commonly recognised best practice. We have also refined our performance development framework.

We commissioned a follow-up staff climate survey to measure the effect these initiatives have had. It is pleasing to note that there was a significant improvement in CCMAU's overall performance index. Our aim is to move CCMAU into the upper quartile of all organisations that participate in the survey.

At year end we moved to temporary accommodation while our existing offices are refurbished. Plans are well advanced to create the best possible physical environment for when we return later in 2005/06.

CCMAU employed 21 staff as at 30 June 2005, with one vacancy. Of the total staff, one was seconded to a ministerial office. Staff turnover was 30.0% (45.9% in 2003/04) and the average length of service is now 2.74 years (2.66 years in 2003/04).

**CCMAU EEO 2005 - GENDER**



### Improving communications and stakeholder relationships

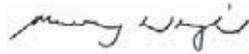
Positive stakeholder relationships and timely and constructive feedback are vital to ensuring CCMAU's outputs make a difference. Throughout the year, Vote Ministers continued to express satisfaction with the quality of our advice.

The Cabinet reshuffle mid-year resulted in changes to our two Vote Ministers. We provided both with briefings on their new portfolios immediately after they received their warrants.

We have continued to receive requests to host visits from other jurisdictions keen to understand how we monitor the companies the Government owns. In 2004/05 we hosted delegations from Western Samoa, the United Kingdom, China, Malaysia, Namibia and the Cook Islands.

As part of CCMAU's drive to ensure the Crown's ownership, monitoring and governance practices align with international best practice, we have moved to strengthen networks with relevant international jurisdictions, with a project to establish an international knowledge and best-practice sharing network. A major highlight of the year was the inaugural meeting of an international practitioners' network of CCMAU-like organisations held in Singapore. CCMAU was instrumental in arranging this meeting and has a mandate to take a leadership role in the network over the next two years. At this stage we have agreement from 25 other CCMAU-like agencies that have agreed to participate in the proposed network.

During the year we changed the layout of our website, making it even easier to navigate. The site has links to the companies and entities we monitor, enabling the public to get a wide appreciation of their activities and performance.



Murray Wright  
Executive Director



CCMAU leadership team –  
Murray Wright, Steve  
Rich, Janine Stewart and  
Michael Moore (absent  
Adrian Wimmers and  
James Cunningham)

## OUTPUT PERFORMANCE – CCMAU

Statement of Objectives and Service Performance  
section 35(3) Public Finance Act 1989

### VOTES AT A GLANCE

Actual expenditure for 2004/05 by output class:



(Figures are GST inclusive)

### VOTE CROWN RESEARCH INSTITUTES

Crown Company Monitoring Advice to the Minister for Crown Research Institutes and Minister of Research, Science and Technology

This class of outputs involves the provision of policy and ownership monitoring advice on nine CRIs and the New Zealand Venture Investment Fund Limited (VIF), and includes:

- advising the Minister for CRIs and the Minister of Research, Science and Technology (RS&T) on the strategic direction of CRIs and VIF respectively, and the commercial and fiscal risks associated with Crown ownership
- providing advice which assists the Minister for CRIs and the Minister of RS&T to set ownership objectives and targets for CRIs and VIF
- monitoring and advising the Minister for CRIs and the Minister of RS&T of CRIs' and VIF's performance against these objectives and targets
- providing policy advice on, and managing issues arising out of, the ownership of CRIs and VIF, including residual implementation issues
- managing, on behalf of the responsible Ministers, the appointment of CRI and VIF directors and monitoring the performance of those directors and boards
- assisting the responsible Ministers in the formulation of shareholders' expectations in relation to the governance practices and structures companies adopt.

Maintaining and enhancing the Crown's ownership interest in these entities contribute to the efficient management of the Crown's assets and liabilities. The CRIs and VIF have an important role to play in the New Zealand innovation system, thereby contributing to improving New Zealand's overall economic performance.

### Significant work completed during the year

- Completion of the 2004/05 CRI strategic planning round, which includes analysing and reporting on each company's draft Statement of Corporate Intent (SCI) and strategic plan so that shareholding Ministers are able to provide informed feedback to boards.
- Involvement in the assessment of AgResearch Ltd's (AgResearch's) campus redevelopment plan, the review of the Institute of Geological and Nuclear Sciences' Ltd's National Isotope Centre, the development of the Ocean Survey 20/20 strategy for New Zealand, the review of organisational and purchasing structure arrangements supporting New Zealand's weather forecasting and climate services provided by MetService and NIWA, the assessment of Industrial Research Ltd's application for \$5 million from the EIF, the review of the future structure and rationale for CRI non-specific output funding, the assessment of the proposed National Centre for Emerging Diseases and Biosecurity, the establishment of the Seed Capital Investment Fund, the establishment of an agribiotechnology VIF seed fund involving AgResearch, and the establishment of REANNZ.
- Securing ministerial agreement on the recycling of CRI dividends within the innovation system.
- Providing a briefing to the new Minister for CRIs as a result of a Cabinet reshuffle mid-year.
- Contributing to the 2005 Operating Framework for CRIs including company-specific addenda for the first time.
- Resolution of the Crown's contribution to the cost of cleaning up a contaminated site at the Institute of Environmental Science and Research Ltd's Mt Eden site.
- Involvement in MoRST's "Picking up the Pace" agenda for improving the science system.
- Completion of the 2005/06 CRI director appointment round, completion of a directors' fees review for 2005/06, co-hosting a seminar for Māori business people, active participation in the wider governance officials' forum, co-hosting a prospective directors' seminar with Te Puni Kōkiri and hosting one ourselves, hosting one-day induction seminars for newly appointed CRI directors, and continuing to provide assistance to other agencies regarding nominations.

### Service performance

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <p>The Minister for CRIs or the Minister of RS&amp;T will expect advice to demonstrate a sound knowledge of the business, the environment within which the CRI or VIF operates and the consequences of shareholder or CRI or VIF actions.</p> <p>All reports will comply with the generic quality standards for analysis and advice outlined on page 133. Output quality will be assessed as follows:</p> <ul style="list-style-type: none"> <li>• The Ministers will expect CCMAU to implement suitable quality control procedures to support the expectations for analysis and advice delivered under the relevant Votes.</li> <li>• Managerial and peer (internal and external, where appropriate) review will be maintained to ensure that the quality standards are met.</li> <li>• The Ministers will be formally requested, on a quarterly basis, to indicate their level of satisfaction with the overall quality of the outputs produced.</li> </ul>	<p>✓</p> <p>✓</p> <p>More than satisfied</p>
<p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister for CRIs and the Executive Director of CCMAU (as amended from time to time) for 2004/05.</p> <p>Quarterly and end-of-year reporting will enable the Minister to assess actual performance in output delivery against those expectations.</p>	<p>✓</p> <p>✓</p>

<p><b>Coverage</b></p> <p>A comprehensive range of services will be provided as agreed with the Minister for CRIs. These will include the capacity to react quickly and provide support for the Minister in Cabinet committees, including relevant briefings on significant issues and regular evaluation of the impacts of shareholder decisions and company actions on the Government’s desired outcomes.</p> <p><b>Cost Effectiveness</b></p> <p>Analysis and advice will be delivered within the cost parameters agreed with the Minister for CRIs (or as subsequently modified by agreement).</p> <p><b>Timeliness</b></p> <p>Timeframes will be agreed between the Minister and the Executive Director of CCMAU for the financial year.</p> <ul style="list-style-type: none"> <li>• Advice will be delivered within the agreed and/or statutory timeframe so that Ministers have sufficient time to consider the issues and take appropriate action. Where agreed deadlines will not be met, extensions are to be formally requested.</li> <li>• Ministerial correspondence (MCs), parliamentary questions (PQs), Cabinet agendas and Official Information Act requests (OIAs) will be responded to within agreed and/or statutory timeframes.</li> <li>• CCMAU will respond appropriately to requests for attendance at Parliament during debates and at Cabinet and select committee meetings.</li> <li>• Quarterly and end-of-year reporting will enable the Minister to assess actual performance in the timeliness of output delivery against those expectations.</li> </ul>	<p>✓</p> <p>✓</p> <p>✓</p> <p>✓<sup>1</sup></p> <p>✓</p> <p>✓</p>
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2004/05	PQs	MCs	OIAs
Estimated	100-130	30-50	4-8
Actual draft replies	43	44	6
% answered by due date	98	93	100

**Cost (\$000)**

2004/05 Actual	1,077
Supp. Est - Voted	1,159
Main Est.	1,183
2003/04 Actual	1,004

(Figures are GST inclusive)

Output class expenditure was \$82,000 or 7% under Supplementary Estimates owing to staff variances and lower consultant costs.

The appropriation for this output class was decreased by \$24,000 in the Supplementary Estimates owing to a fiscally neutral transfer to Vote SOEs reflecting the allocation of overhead costs between the two Votes that fund CCMAU, offset by an increase to cover the costs of the State Sector Retirement Savings Scheme.

1 The timeliness of responses was occasionally affected by the large volume of information sought, the complexity of the issues involved and/or the need to consult with the relevant SOE, Crown company or Crown entity to obtain additional information. In some cases, where necessary, extensions of time were obtained. In other cases, where there was a large amount of correspondence on the same subject, delays occurred while a generic response was agreed with the Minister.



## VOTE STATE-OWNED ENTERPRISES

### Crown Company Monitoring Advice to the Minister for State-Owned Enterprises and Other Responsible Ministers

This class of outputs involves the provision of policy and ownership monitoring advice on the SOEs, Crown companies and Crown entities covered by Vote SOEs (collectively referred to below as "SOEs"). This includes:

- advising the Minister for SOEs and other responsible Ministers on the strategic direction of SOEs; the commercial and fiscal risks associated with Crown ownership; proposals to establish and restructure SOEs; and the processes and outcomes of significant SOE divestments and acquisitions
- providing advice which assists Ministers to set ownership objectives and targets for SOEs
- monitoring and advising Ministers of SOEs' performance against these objectives and targets
- providing policy advice on, and managing issues arising out of, the ownership of SOEs, including residual implementation issues
- managing, on behalf of responsible Ministers, the appointment of SOE directors and monitoring the performance of those directors and boards
- assisting responsible Ministers in the formulation of shareholders' expectations in relation to the governance practices and structures companies adopt.

Maintaining and enhancing the Crown's ownership interest in these entities contribute to the efficient management of the Crown's assets and liabilities.

#### Significant work completed during the year

- Completion of the 2004/05 SOE business planning round, which includes analysing and reporting on each company's draft SCI and business plan so that shareholding Ministers are able to provide informed feedback to boards.
- Completion of long-term hold owner's reviews for MetService, Landcorp, Meridian and Solid Energy; and the commencement of reviews for AgriQuality,ASURE and Airways.
- Involvement in the review of organisational and purchasing structure arrangements supporting New Zealand's weather forecasting and climate services provided by MetService and NIWA.
- Providing a briefing to the new Minister for SOEs as a result of a Cabinet reshuffle mid-year.
- Assessment of a number of business cases including Invercargill Airport's runway extension, Kiwibank's expansion into the small business banking market, New Zealand Post's Express and Logistics Group joint venture with DHL, Genesis' e3p project, and a major transaction for Solid Energy (with Toll Holdings Ltd).
- Establishment of a framework to incentivise TVNZ to achieve its cost of capital and be able to reinvest surpluses over and above it.
- Managing a number of company issues, and the provision of advice to Ministers on them, including electricity security of supply issues, qualified audit opinion for THL, Transpower's proposed grid upgrade

through the upper North Island, Meridian’s concerns over the Waitaki Water Allocation Board’s draft proposal, Landcorp’s proposed sale of two properties in the greater Wellington region, carbon tax impacts across the energy sector, and environmental mining issues affecting Solid Energy.

- Progressing value-based reporting of company and entity performance.
- Convening of an SOE Chairs’ meeting in May with the Minister for SOEs and other Ministers.
- Completion of a governance review for Animal Control Products Ltd.
- Completion of significant SOE appointment rounds, completion of a directors’ fees review for 2005/06, co-hosting a seminar for Māori business people, active participation in the wider governance officials’ forum, co-hosting a prospective directors’ seminar with Te Puni Kōkiri and hosting one ourselves, hosting one-day induction seminars for newly appointed SOE directors, and continuing to provide assistance to other agencies regarding nominations.

**Service performance**

Performance Dimensions	Achieved?
<p><b>Quality</b></p> <p>The Minister for SOEs and other responsible Ministers will expect advice to demonstrate a sound knowledge of the Crown company’s business, the environment within which the company operates and the consequences of shareholder or company actions.</p> <p>All reports will comply with the generic quality standards for analysis and advice outlined on page 133. Output quality will be assessed as follows:</p> <ul style="list-style-type: none"> <li>• The Minister will expect CCMAU to implement suitable quality control procedures to support the expectations for analysis and advice delivered under the relevant Votes. ✓</li> <li>• Managerial and peer (internal and external, where appropriate) review will be maintained to ensure that the quality standards are met. ✓</li> <li>• The Minister will be formally requested, on a quarterly basis, to indicate his level of satisfaction with the overall quality of the outputs produced. More than satisfied</li> </ul> <p><b>Quantity</b></p> <p>The quantity and nature of advice and operational services will be supplied on the basis agreed between the Minister of Finance and the Secretary to the Treasury (as amended from time to time) for 2004/05. ✓</p> <p>Quarterly and end-of-year reporting will enable the Minister to assess actual performance in output delivery against those expectations. ✓</p> <p><b>Coverage</b></p> <p>A comprehensive range of services will be provided as agreed with the Minister for SOEs. These will include the capacity to react quickly and provide support for the Minister in Cabinet committees, including relevant briefings on significant issues and regular evaluation of the impacts of shareholder decisions and company actions on the Government’s desired outcomes. ✓</p> <p><b>Cost Effectiveness</b></p> <p>Analysis and advice will be delivered within the cost parameters agreed with the Minister for SOEs (or as subsequently modified by agreement). ✓</p>	

### Timeliness

Timeframes will be agreed between the Minister and the Executive Director of CCMAU for the financial year.

- Advice will be delivered within the agreed and/or statutory timeframe so that Ministers have sufficient time to consider the issues and take appropriate action. Where agreed deadlines will not be met, extensions are to be formally requested. ✓
- Ministerial correspondence (MCs), parliamentary questions (PQs), Cabinet agendas and Official Information Act requests (OIAs) will be responded to within agreed and/or statutory timeframes. ✓<sup>1</sup>
- CCMAU will respond appropriately to requests for attendance at Parliament during debates and at Cabinet and select committee meetings. ✓
- Quarterly and end-of-year reporting will enable the Minister to assess actual performance in the timeliness of output delivery against those expectations. ✓

2004/05	PQs	MCs	OIAs
Estimated	120-160	80-120	12-20
Actual draft replies	135	182	17
% answered by due date	99	77	76

### Cost (\$'000)

2004/05 Actual	2,543
Supp. Est - Voted	2,648
Main Est.	2,588
2003/04 Actual	2,364

(Figures are GST inclusive)

Output class expenditure was \$105,000 or 4% under Supplementary Estimates owing largely to personnel cost savings. The appropriation for this output class was increased by \$60,000 due to a fiscally neutral transfer from Vote CRIs to cover the distribution of corporate costs between the two votes that fund CCMAU and to cover the costs of the State Sector Retirement Savings Scheme.

<sup>1</sup> The timeliness of responses was occasionally affected by the large volume of information sought, the complexity of the issues involved and/or the need to consult with the relevant SOE, Crown company or Crown entity to obtain additional information. In some cases, where necessary, extensions of time were obtained. In other cases, where there was a large amount of correspondence on the same subject, delays occurred while a generic response was agreed with the Minister.

# FINANCIAL STATEMENTS

for the year ended 30 June 2005

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## STATEMENT OF RESPONSIBILITY

Pursuant to sections 35 and 37 of the Public Finance Act 1989 (which, in accordance with section 33 of the Public Finance Amendment Act 2004 (PFAA), continues to apply to the year ended 30 June 2005 as if they had not been amended by the PFAA), the Secretary to the Treasury is responsible for the preparation of the Department's financial statements and non-departmental supplementary schedules, and the judgements made in the process of producing these financial statements and supplementary schedules.

The Department's internal control procedures provide reasonable assurance as to the integrity and reliability of its financial reporting.

In the opinion of the Secretary to the Treasury:

- the Department's financial statements fairly reflect the financial position and operations for the financial year ended 30 June 2005
- the supplementary schedules fairly reflect the assets, liabilities, contingencies and commitments managed by the Treasury on behalf of the Crown as at 30 June 2005 and revenues and expenses managed by the Treasury on behalf of the Crown for the year ended on that date.



John Whitehead  
Secretary to the Treasury

21 September 2005



John Matheson  
Chief Financial Officer  
(countersigned)

21 September 2005

# FINANCIAL STATEMENTS – DEPARTMENTAL

for the year ended 30 June 2005

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# OVERVIEW OF DEPARTMENTAL FINANCIAL RESULTS

for the year ended 30 June 2005

The following significant movements in actual results between 2004/05 and 2003/04 are explained below.

	2005 Actual \$000	2004 Actual \$000
<b>Revenue</b>		
Revenue Crown	51,153	52,445
Other revenue	734	510
<b>Expenses</b>		
Personnel costs	33,423	31,507
Operating costs	14,310	16,822
Consultants	1,996	2,783
Capital charge	630	461
<b>Non-current assets</b>		
Property, plant and equipment	6,116	4,247
<b>Taxpayers' funds</b>		
General funds	8,927	7,127

## Revenue

**Revenue Crown** for departmental outputs decreased by \$1.3 million, mainly due to reductions in funding for:

- national rail outputs following the completion of the purchase of rail infrastructure during 2003/04 and
- accommodation project operating costs as the project was completed in December 2004.

**Other revenue** increased by \$0.2 million due mainly to a full year's funding for SSRSS of \$0.4 million, which was introduced in April 2004. Partly offsetting this increase was a reduction in study bond repayment receipts of \$0.1 million and other minor movements.

## Expenditure

**Personnel costs** increased by \$1.9 million due mainly to a 2.5% market increase in salaries and an increase in staff numbers.

**Operating costs** decreased by \$2.5 million due mainly to:

- process management services expenditure reducing by \$2.1 million mainly from work on the national rail project winding down and completion of a one-off review of New Zealand House in 2003/04
- furniture purchases being capitalised from 1 July 2004 following a change in the application of the Department's capitalisation policy (\$0.5 million)
- write-off of leasehold improvements in 2003/04 (\$0.1 million)

which were partly offset by:

- increases in fees to auditors (\$0.2 million)
- adjustment to the provision for onerous leases (\$0.1 million)
- increase in transport and travel costs of \$0.1 million due largely to increased work on trade policy, international public sector accounting standards and harmonisation of national accounts.

The remaining variance in operating costs is spread over a number of operating cost items.

**Consultants** decreased by \$0.8 million due largely to the Maui gas redetermination project being completed during 2003/04.

**Capital charge** increased by \$0.2 million due to increased taxpayers' equity following capital contributions of \$1.8 million during 2004/05 for the capital costs of the accommodation project.

#### Non-Current Assets

**Property, plant and equipment** increased by \$1.9 million due mainly to the capitalisation of leasehold improvements on completion of the accommodation project during 2004/05.

#### Taxpayers' Funds

**General funds** increased by \$1.8 million due to capital contributions during 2004/05 for the capital costs of the accommodation project.

# STATEMENT OF FINANCIAL PERFORMANCE

for the year ended 30 June 2005

The Statement of Financial Performance details the revenue and expenses relating to all outputs (goods and services) produced by the Department, including CCMAU, during the financial year ended 30 June 2005. Total Expenses plus GST equals Total Departmental Output Classes Expenditure and Appropriations in the Statement of Expenditure and Appropriations on page 98.

2004 Actual \$000		Notes	2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
<b>Revenue</b>					
52,445	Crown	1	51,153	54,009	52,335
510	Other revenue	2	734	351	1,002
<b>52,955</b>			<b>51,887</b>	<b>54,360</b>	<b>53,337</b>
<b>Expenses</b>					
31,507	Personnel costs		33,423	31,776	33,733
16,822	Operating costs	3	14,310	16,289	14,992
2,783	Consultants		1,996	4,115	2,402
1,382	Depreciation	4	1,528	1,525	1,580
461	Capital charge	5	630	655	630
<b>52,955</b>			<b>51,887</b>	<b>54,360</b>	<b>53,337</b>
-	<b>Net Surplus</b>		-	-	-

*The accounting policies on pages 99 to 101 and accompanying notes on pages 102 to 106 are an integral part of these financial statements.*

# STATEMENT OF MOVEMENTS IN TAXPAYERS' FUNDS

for the year ended 30 June 2005

The Statement of Movements in Taxpayers' Funds combines information about the net surplus with other aspects of the financial performance of the Department, including CCMAU, to give a degree of measure of comprehensive income.

2004 Actual \$000		2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
5,427	Taxpayers' funds at the beginning of the year	7,127	7,327	7,127
	Movements during the year			
-	Net surplus	-	-	-
-	<b>Total Recognised Revenues and Expenses for the Year</b>	-	-	-
1,700	Capital contribution from the Crown	1,800	1,800	1,800
<b>7,127</b>	<b>Taxpayers' Funds at the End of the Year</b>	<b>8,927</b>	<b>9,127</b>	<b>8,927</b>

*The accounting policies on pages 99 to 101 and accompanying notes on pages 102 to 106 are an integral part of these financial statements.*

# STATEMENT OF FINANCIAL POSITION

as at 30 June 2005

The Statement of Financial Position reports the total assets and liabilities of the Department, including CCMAU, as at 30 June 2005. Taxpayers' funds are represented by the difference between the assets and liabilities.

2004 Actual \$000		Notes	2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
	<b>Taxpayers' Funds</b>				
7,127	General funds		8,927	9,127	8,927
<b>7,127</b>	<b>Total Taxpayers' Funds</b>		<b>8,927</b>	<b>9,127</b>	<b>8,927</b>
	Represented by:				
	<b>Assets</b>				
	Current assets				
4,050	Cash and bank balances		3,261	2,005	3,179
363	Advances and prepayments		581	437	364
247	Accounts receivable		324	106	377
6,913	Debtor - Crown		5,653	6,402	5,954
<b>11,573</b>			<b>9,819</b>	<b>8,950</b>	<b>9,874</b>
	Non-current assets				
4,247	Property, plant and equipment	6	6,116	6,368	6,372
<b>4,247</b>			<b>6,116</b>	<b>6,368</b>	<b>6,372</b>
<b>15,820</b>	<b>Total Assets</b>		<b>15,935</b>	<b>15,318</b>	<b>16,246</b>
	Less:				
	<b>Liabilities</b>				
	Current liabilities				
4,790	Payables and accrued expenses		3,082	2,393	3,682
3,395	Provision for employee entitlements	7	3,509	3,253	3,179
91	Provision for onerous contracts	8	30	43	30
<b>8,276</b>			<b>6,621</b>	<b>5,689</b>	<b>6,891</b>
	Non-current liabilities				
347	Provision for employee entitlements	7	358	433	381
70	Provision for onerous contracts	8	29	69	47
<b>417</b>			<b>387</b>	<b>502</b>	<b>428</b>
<b>8,693</b>	<b>Total Liabilities</b>		<b>7,008</b>	<b>6,191</b>	<b>7,319</b>
<b>7,127</b>	<b>Net Assets</b>		<b>8,927</b>	<b>9,127</b>	<b>8,927</b>

*The accounting policies on pages 99 to 101 and accompanying notes on pages 102 to 106 are an integral part of these financial statements.*

# STATEMENT OF CASH FLOWS

for the year ended 30 June 2005

The Statement of Cash Flows summarises the cash movements in and out of the Department during the financial year. It takes no account of money owed to the Department or owing by the Department and therefore differs from the Statement of Financial Performance on page 92.

2004 Actual \$000		Notes	2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
	<b>Cash Flow from Operating Activities</b>				
	Cash was provided from:				
51,591	Supply of outputs to the Crown		52,413	54,539	53,294
488	Supply of outputs to third parties		739	351	1,002
<b>52,079</b>			<b>53,152</b>	<b>54,890</b>	<b>54,296</b>
	Cash was disbursed to:				
32,181	Personnel costs		33,298	31,594	33,858
18,804	Operating costs		18,617	20,899	18,742
461	Capital charge		630	655	630
<b>51,446</b>			<b>52,545</b>	<b>53,148</b>	<b>53,230</b>
<b>633</b>	<b>Net Cash Flow from Operating Activities</b>	9	<b>607</b>	<b>1,742</b>	<b>1,066</b>
	<b>Cash Flow from Investing Activities</b>				
	Cash was provided from:				
-	Sale of property, plant and equipment		3	2	3
	Cash was disbursed to:				
(3,574)	Purchase of property, plant and equipment		(3,199)	(2,676)	(3,740)
<b>(3,574)</b>	<b>Net Cash Flow from Investing Activities</b>		<b>(3,196)</b>	<b>(2,674)</b>	<b>(3,737)</b>
	<b>Cash Flow from Financing Activities</b>				
	Cash was provided from:				
1,700	Capital contributions		1,800	1,800	1,800
<b>1,700</b>	<b>Net Cash Flow from Financing Activities</b>		<b>1,800</b>	<b>1,800</b>	<b>1,800</b>
<b>(1,241)</b>	<b>Net (Decrease)/Increase in Cash and Bank Balances</b>		<b>(789)</b>	<b>868</b>	<b>(871)</b>
5,291	Cash and bank balances at the beginning of the year		4,050	1,137	4,050
<b>4,050</b>	<b>Cash and Bank Balances at the End of the Year</b>		<b>3,261</b>	<b>2,005</b>	<b>3,179</b>

*The accounting policies on pages 99 to 101 and accompanying notes on pages 102 to 106 are an integral part of these financial statements.*

## STATEMENT OF COMMITMENTS

as at 30 June 2005

The Department has a non-cancellable lease on its principal premises at No. 1 The Terrace, Wellington. The Department also has a non-cancellable lease over office space in Boulcott Street, Wellington. The Department has other operating commitments consisting of computer maintenance contracts, building services contracts and contracts for services. These operating lease commitments have been recorded at their gross values in the Statement of Commitments. However, onerous contract provisions have been recorded for the office space the Department does not occupy, which is detailed in Note 8.

The Department's 2004 capital commitments relate to the accommodation project.

2004 Actual \$000		2005 Actual \$000
	<b>Operating Lease Commitments</b>	
4,922	Less than one year	3,656
3,215	One to two years	3,234
9,546	Two to five years	8,861
31,299	Greater than five years	20,362
<b>48,982</b>		<b>36,113</b>
2,489	Capital Commitments	-
<b>51,471</b>	<b>Total Commitments</b>	<b>36,113</b>

*The accounting policies on pages 99 to 101 and accompanying notes on pages 102 to 106 are an integral part of these financial statements.*

# STATEMENT OF CONTINGENT ASSETS AND LIABILITIES

as at 30 June 2005

As at 30 June 2005, the Department had no departmental contingent assets or liabilities (30 June 2004: nil).

*The accounting policies on pages 99 to 101 and accompanying notes on pages 102 to 106 are an integral part of these financial statements.*

# STATEMENT OF EXPENDITURE AND APPROPRIATIONS

for the year ended 30 June 2005

The Statement of Expenditure and Appropriations details expenditure (GST inclusive where applicable) against appropriations. Total Departmental Output Classes Expenditure and Appropriations less GST equals total expenses in the Statement of Financial Performance on page 92.

2004 Actual \$000		2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
	<b>Vote Finance: Departmental Output Classes</b>			
3,983	Policy Advice: General Economic and Fiscal Strategies	4,469	5,427	4,568
	Policy Advice: Financial and Public Sector Management Systems			
3,507		3,382	4,327	3,659
1,859	Policy Advice: Tax	2,670	2,767	2,696
2,241	Budget Management	2,763	2,338	2,774
6,914	Economic and Fiscal Forecasting and Reporting	6,809	6,303	7,014
5,274	Debt and Related Financial Asset Management*	4,745	5,623	4,969
	Management of Claims Against the Crown, Contractual Liabilities and Crown Properties			
4,163		2,582	4,147	2,872
	Policy Advice: Ownership and Performance of Crown Companies and Financial Institutions			
2,904		3,007	3,292	3,070
	Policy Advice: Regulation and Vote Purchase, Ownership and Performance Issues			
25,363		24,328	23,159	24,575
<b>56,208</b>		<b>54,755</b>	<b>57,383</b>	<b>56,197</b>
	<b>Vote Crown Research Institutes: Departmental Output Classes</b>			
	Crown Company Monitoring Advice to the Minister for Crown Research Institutes			
1,004		1,077	1,183	1,159
	<b>Vote State-Owned Enterprises: Departmental Output Classes</b>			
	Crown Company Monitoring Advice to the Minister for State-Owned Enterprises and Other Responsible Ministers			
2,364		2,543	2,588	2,648
<b>59,576</b>	<b>Total Departmental Output Classes Expenditure and Appropriations</b>	<b>58,375</b>	<b>61,154</b>	<b>60,004</b>
	<b>Vote Finance: Capital Contributions to the Department</b>			
	Capital investment			
1,700		1,800	1,800	1,800
<b>61,276</b>	<b>Total Departmental Expenditure and Appropriations</b>	<b>60,175</b>	<b>62,954</b>	<b>61,804</b>

*The accounting policies on pages 99 to 101 and accompanying notes on pages 102 to 106 are an integral part of these financial statements.*

\* Appropriated under permanent legislative authority.

# STATEMENT OF ACCOUNTING POLICIES

## Reporting entity and statutory base

These are the financial statements of the Treasury, a government department (the “Department”) as defined by section 2 of the Public Finance Act 1989 for the financial year ended 30 June 2005. The statements have been prepared pursuant to section 45 of that Act, which, in accordance with section 33 of the Public Finance Amendment Act 2004 (PFAA), continues to apply to the year ended 30 June 2005 as if they had not been amended by the PFAA.

The activities of CCMAU have been incorporated into these financial statements.

## Measurement system

These financial statements have been prepared on the basis of historical cost.

## Accounting policies

### Revenue

The Department derives revenue through the provision of outputs to the Crown and for services to third parties. Such revenue is recognised in the Statement of Financial Performance when earned.

### Cost allocation

The Department has derived the cost of outputs using a cost allocation system, which is outlined below.

### Definition of terms

“Branch” is a cost centre that directly and indirectly contributes to outputs.

“Corporate overhead costs” are those costs attributed to support service cost centres.

“Direct costs” are costs that can be identified with a single output.

“Indirect costs” are costs that cannot be identified with an output in an economically feasible manner. They are incurred for the common benefit of more than one output.

### Corporate overhead costs

Corporate overhead costs are assigned to branches on an approximate resource usage basis.

### Direct costs

Where possible, costs are assigned directly to outputs.

### Direct labour costs

A time recording system is used to collect and assign direct labour costs to outputs.

### Indirect costs

Indirect costs, including corporate overhead costs, are allocated to outputs on a direct labour cost basis.

## Accounts receivable

Accounts receivable are recorded in the Statement of Financial Position at the amounts expected to be ultimately collected.

## Leases

The Department leases office premises. Substantially all the risks and benefits of ownership are retained by the lessor and therefore these leases are classified as operating leases. Operating lease costs are recognised as an expense in the Statement of Financial Performance in the year in which they are incurred, except for onerous lease provisions.

## Property, plant and equipment

Property, plant and equipment are stated at the lower of cost less accumulated depreciation or fair value. All computer equipment assets and all other assets costing more than \$5,000 are capitalised.

## Depreciation

Depreciation of property, plant and equipment is provided on a straight line basis so as to allocate the cost of assets, less their estimated residual value, over their useful lives. The estimated economic useful lives are:

Furniture and fittings:	Safes	15 years
	Shelving	10 years
	Other	5 years
Leasehold improvements:		12 years
Office machinery and electrical equipment:	Photocopiers	5 years
	Other	5 years
	Electronic white boards	3 years
	Facsimile machines	3 years
Computer equipment:	UPS/Air conditioning	5 years
	Hardware	5 years
	Cabling	5 years
	System software	3 years
	PCs, terminals and printers	3 years
Plant:		5 years

## Provisions

### Employee entitlements

Provision is made in respect of the Department's liability for resigning, retirement and long service leave. These provisions have been calculated on an actuarial basis based on the present value of expected future entitlements.

### Onerous contract

Where the benefits expected to be derived from a contract are lower than the unavoidable costs of meeting the Department's obligation under the contract, a provision is recognised. The provision is stated at the present value of the future net cash outflows expected to be incurred in respect of the contract.

### Foreign currency

Foreign currency transactions, relating primarily to information, travel and training costs, are reported at the New Zealand dollar exchange rate at the date of the transaction.

## Financial instruments

Financial instruments primarily comprise cash and bank balances, receivables and payables. All financial instruments are recognised in the Statement of Financial Position. Revenues and expenses in relation to all financial instruments are recognised in the Statement of Financial Performance.

## Goods and services tax

Amounts in the financial statements are reported exclusive of GST except for:

- advances and prepayments, accounts receivable, debtor – Crown and payables
- figures in the Statement of Expenditure and Appropriations where applicable.

The amount of GST owing to or from the Inland Revenue Department as at balance date, being the difference between output GST and input GST, is included in the Statement of Financial Position as either a payable or a receivable (as appropriate).

## Income tax

Government departments are exempt from the payment of income tax in terms of the Income Tax Act 1994. Accordingly, no charge for income tax has been provided for.

## Commitments

Commitments disclosed include those operating and capital commitments arising from non-cancellable contractual obligations.

## Contingent assets and liabilities

Departmental contingent assets and liabilities are disclosed in the Statement of Contingent Assets and Liabilities at the point at which the contingency is evident.

## Changes in accounting policies

There have been no changes in accounting policies, including cost allocation accounting policies, since the date of the last audited financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 30 June 2005

## 1 Revenue – Crown

This is revenue earned for the supply of outputs to the Crown.

## 2 Other revenue

2004 Actual \$000		2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
186	Rental income	186	186	186
36	Court costs awarded	-	-	-
123	Study bond repayments	-	-	-
100	State Sector Retirement Superannuation Scheme	489	100	479
65	Miscellaneous	59	65	337
510		734	351	1,002

## 3 Operating costs

2004 Actual \$000		2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
5,400	Lease of premises	5,322	5,207	5,132
117	Fees to KPMG for audit of the Department and NZDMO	250	127	253
118	Fees to Auditor-General for audit of Crown financial statements	130	120	120
65	Other fees to Department and NZDMO auditors	147	163	124
193	Other fees to Crown auditors	200	240	266
105	Write-offs - leasehold improvements	-	-	-
(157)	Provisions for onerous leases	(9)	(43)	(9)
3,840	Process management services	1,704	2,642	1,834
1,208	Transport and travel	1,313	1,150	1,241
771	Training and development	840	900	837
778	Information costs	825	793	773
648	Data processing costs	709	654	628
521	Furniture/Office equipment purchases	66	701	61
3,215	Other operating costs	2,813	3,635	3,732
16,822		14,310	16,289	14,992

## 4 Depreciation

2004 Actual \$000		2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
20	Furniture and fittings	135	17	137
142	Leasehold improvements	397	365	412
117	Office machinery and electrical equipment	43	104	44
1,102	Computer equipment	952	1,038	986
1	Plant	1	1	1
<b>1,382</b>		<b>1,528</b>	<b>1,525</b>	<b>1,580</b>

## 5 Capital charge

The Treasury pays a capital charge to the Crown on its average taxpayers' funds for the six months ended 30 June and 31 December. The capital charge rate for the financial year ended 30 June 2005 was 8% (30 June 2004: 8.5%).

## 6 Property, plant and equipment

The following categories of property, plant and equipment were used by the Department.

2004 Actual \$000		2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
	<b>Furniture and fittings</b>			
509	Cost	1,002	595	1,168
(459)	Accumulated depreciation	(213)	(479)	(382)
50		789	116	786
	<b>Leasehold improvements</b>			
3,042*	Cost	4,592	6,325	4,647
(404)	Accumulated depreciation	(430)	(1,734)	(535)
2,638		4,162	4,591	4,112
	<b>Office machinery and electrical equipment</b>			
1,097	Cost	750	1,076	1,082
(978)	Accumulated depreciation	(708)	(1,076)	(1,006)
119		42	-	76
	<b>Computer equipment</b>			
7,508	Cost	6,928	8,954	7,987
(6,069)	Accumulated depreciation	(5,805)	(7,293)	(6,589)
1,439		1,123	1,661	1,398
	<b>Plant</b>			
5	Cost	-	5	-
(4)	Accumulated depreciation	-	(5)	-
1		-	-	-
<b>4,247</b>	<b>Total Property, Plant and Equipment</b>	<b>6,116</b>	<b>6,368</b>	<b>6,372</b>

\* The 30 June 2004 actual cost balance included \$716,000 of work in progress which has since been classified as leasehold improvements and depreciated.

## 7 Provision for employee entitlements

2004 Actual \$000		2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
1,311	Retirement, resigning and long service leave	1,285	1,533	1,413
1,970	Annual leave	2,058	1,951	1,739
249	Accrued salaries	314	-	208
179	Accrued performance payments	139	202	200
33	Accrued other entitlements	71	-	-
<b>3,742</b>		<b>3,867</b>	<b>3,686</b>	<b>3,560</b>
	Represented by:			
3,395	Current	3,509	3,253	3,179
347	Non-current	358	433	381
<b>3,742</b>		<b>3,867</b>	<b>3,686</b>	<b>3,560</b>

## 8 Provision for onerous contracts

2004 Actual \$000		2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
423	Balance at the beginning of the year	161	161	161
(157)	Amount reversed	(9)	-	-
(105)	Amount utilised	(93)	(49)	(84)
<b>161</b>		<b>59</b>	<b>112</b>	<b>77</b>
	Represented by:			
91	Current	30	43	30
70	Non-current	29	69	47
<b>161</b>		<b>59</b>	<b>112</b>	<b>77</b>

The Department has a non-cancellable lease. This is at Level 14, 47 Boulcott Street in Wellington. Owing to a change in its activities, the Department no longer occupies Level 14 at the Boulcott Street premises. This premise, which was previously sub-leased, is now vacant. Owing to market conditions, the anticipated rental income is expected to be much lower than the rental expense being incurred. The net obligation under the lease agreements has been provided for as an onerous contract and this liability will be incurred over the next three years.

The 2004 comparatives include a provision in respect to No. 1 The Terrace. However, this provision is no longer required as a new lease for No. 1 The Terrace commenced from 1 July 2005.

## 9 Reconciliation of net surplus to net cash flow from operating activities

This reconciliation discloses the non-cash adjustments applied to the net surplus reported in the Statement of Financial Performance on page 92 to arrive at the net cash flow from operating activities disclosed in the Statement of Cash Flows on page 95.

2004 Actual \$000		2005 Actual \$000	2005 Main Estimates \$000	2005 Supp. Estimates \$000
-	<b>Net Surplus from Statement of Financial Performance</b>	-	-	-
	Non-cash items			
1,382	Depreciation	1,528	1,525	1,580
105	Write-offs - property, plant and equipment	-	-	-
	Working capital movements			
4	(Increase)/decrease in advances and prepayments	(218)	1	-
(168)	(Increase)/decrease in accounts receivable	(77)	(40)	(130)
(854)	Decrease/(increase) in debtor - Crown	1,260	530	959
1,066	(Decrease)/increase in payables, accrued expenses and provisions	(1,991)	(291)	(629)
(645)	Increase/(decrease) in other current liabilities	113	19	(730)
(257)	(Decrease)/increase in non-current liabilities	(29)	-	11
	Investing activity items			
-	Net loss (gain) on sale of property, plant and equipment	21	(2)	5
633	<b>Net Cash Flow from Operating Activities</b>	<b>607</b>	<b>1,742</b>	<b>1,066</b>

## 10 Financial instruments

The Department is party to financial instrument arrangements as part of its everyday operations. These financial instruments include cash and bank balances, advances, accounts receivable, debtor – Crown, and payables and accrued expenses.

### Credit risk

In the normal course of its business the Department is subject to credit risk from debtors other than the Crown.

The Department does not require any collateral or security to support financial instruments with financial institutions with which the Department deals, as these entities have high credit ratings. For its other financial instruments the Department does not have significant concentrations of credit risk.

### Fair value

The fair value of financial instruments is equivalent to the carrying amount disclosed in the Statement of Financial Position.

### Currency and interest rate risk

The Department has no significant exposure to currency exchange loss risk and its financial instruments are not interest rate sensitive.

## 11 Related party information

The Department is a wholly owned entity of the Crown. The Government significantly influences the roles of the Department as well as being its major source of revenue.

The Department enters into numerous transactions with other government departments, Crown agencies and SOEs on an arm's length basis. These transactions are not required to be disclosed as related party transactions.

## 12 Transition to New Zealand Equivalents to International Financial Reporting Standards

The Department will be adopting New Zealand IFRS for the first time in its audited financial statements for the year ending 30 June 2008. This timetable is in line with the adoption of New Zealand equivalents to IFRS in the consolidated financial statements of the Government reporting entity. The Department will be adopting the accounting policies of the financial statements of the Government, which have just been released in draft. The Department will evaluate during 2005/06 the differences, if any, between current policies and the draft policies of the financial statements of the Government. The Treasury has established a team to manage the New Zealand IFRS implementation. At this stage no material issues have been identified. However, the actual impact of adopting New Zealand IFRS may vary from this initial assessment, and the variation may be material.

# SUPPLEMENTARY FINANCIAL SCHEDULES – NON-DEPARTMENTAL

for the year ended 30 June 2005

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The following supplementary financial schedules record the expenses, revenue and capital receipts, assets and liabilities that the Department manages on behalf of the Crown. These supplementary financial schedules include NZDMO balances reported on pages 121 to 130.

The Department administered \$5,025 million of expenses, \$2,799 million of revenue, \$862 million of capital receipts, \$20,939 million of assets and \$52,499 million of liabilities on behalf of the Crown for the year ended 30 June 2005.

The financial information reported in these schedules is consolidated into the Crown financial statements, and therefore readers of these schedules should also refer to the Crown financial statements for the year ended 30 June 2005.

## OVERVIEW

### Air New Zealand

The Crown took up its share of a rights issue by Air New Zealand, at a cost of \$149 million (page 112).

### Coins in circulation liability

The liability for coins issued by the Treasury prior to 1989 and still in circulation was transferred to the Reserve Bank during the year (page 117).

### Dividends

SOE dividends increased by \$102 million from 2003/04, as a result of higher dividends from Meridian, offset by lower dividends from LandCorp Farming, Mighty River Power and Solid Energy. Crown entity dividends increased by \$41 million, as a result of a special dividend from TVNZ. CRI dividends increased by \$15 million, as a result of dividends from NIWA (page 114).

### GSF unfunded liability movement

The GSF and New Zealand Superannuation Corporation liabilities as at 30 June 2005 were \$11,430 million (page 117). This was an increase of \$1,261 million compared with 30 June 2004 (page 110). The primary reasons for the increase were movements in the economic and demographic assumptions used in calculating the liability. From 1 July 2004 the GSF unfunded liability movement has not been appropriated as it is not required to be pursuant to the Public Finance Act 1989 (page 111).

### International Financial Institutions

No capital contributions to the International Monetary Fund (IMF) were required in 2004/05 (page 112), whilst returns of capital totalled \$230 million (page 115). This reflects the cyclical nature of the IMF lending programme.

### Net foreign debt repayment

Foreign currency activity in 2004/05 included \$700 million of additional borrowing to fund \$1,900 million of increased Reserve Bank foreign exchange reserves across a four year period. The related swap activity in 2004/05 together with a net receipt of collateral deposits produced a net foreign borrowing position for 2004/05 (page 115) compared to the net foreign debt repayment for 2003/04 (page 112).

### NPF Defined Benefit Plan (Annuitants) Scheme liability movement

The NPF DBP (A) Scheme liability as at 30 June 2005 was \$944 million (page 117). This was an increase of \$53 million compared with 30 June 2004. The primary reason for the increase was movements in the economic assumptions used in calculating the liability.

### Other Income – NZDMO

This item increased by \$47 million from 2003/04, as a result of higher interest payments to the Crown from Housing New Zealand Corporation and District Health Boards (page 114).

### Reserve Bank

The Reserve Bank received a capital injection of \$1,000 million to enhance its capacity for intervention in foreign exchange markets (page 112).

## Rail issues

The name of the Crown entity which will manage the rail infrastructure had not been determined when appropriations were established for 2004/5. Therefore Track Co was used as a provisional name for appropriation purposes.

During the year, the Crown:

- continued the structural upgrade of Wellington Railway Station, at a cost of \$7 million in 2004/05 (page 112)
- provided a further \$10.4 million of loans to Auckland Regional Council for the purchase and upgrade of commuter rolling stock (page 112). The loans were repaid in full at the end of the year (page 115)
- continued work on double tracking part of the Western line in Auckland, at a cost of \$5 million in 2004/05 (page 112). Funding was provided by a grant from Infrastructure Auckland (page 114)
- transferred responsibility for the Auckland rail corridor (including the double tracking project) to NZRC. Hence no access fee revenue was recorded in 2004/05 (page 114)
- completed the purchase of the rail network assets from Toll NZ Ltd at a cost of \$8 million in 2004/05 (page 112), and transferred some of the assets purchased to NZRC (page 115)
- spent \$50 million (GST inclusive) of the \$200 million (GST exclusive) committed to upgrading the national rail network (page 111). This commitment was re-classified from capital to operating expenses, resulting in an increase in non-cancellable operating commitments and a reduction in capital commitments (page 118)
- provided \$20 million of working capital, and a loan facility for up to \$75 million, to NZRC. \$15 million of the facility had been drawn at the end of the year (page 112), and the balance is expected to be drawn in 2005/06
- provided additional funding of \$6.9 million to NZRC for certain non-recoverable expenditure (page 111). This expenditure was incurred after the Supplementary Estimates had been finalised, and hence was unappropriated (page 113).

# STATEMENT OF ACCOUNTING POLICIES

for the year ended 30 June 2005

Measurement and recognition rules applied in the preparation of these non-departmental supplementary financial schedules are consistent with GAAP and Crown accounting policies.

The financial information reported in these schedules is consolidated into the Crown financial statements, and therefore readers of these schedules should also refer to the Crown financial statements for the year ended 30 June 2005.

# SCHEDULE OF EXPENSES

for the year ended 30 June 2005

The Schedule of Expenses summarises expenses that the Department administers on behalf of the Crown. Details of non-departmental expenditure and appropriations are provided on pages 111 to 112.

2004 Actual \$000		2005 Actual \$000	2005 Supp. Estimates \$000
	<b>Vote Finance</b>		
11,655	Non-departmental output classes	10,261	11,462
749,880	Benefits and other unrequited expenses	827,384	826,418
2,549,901	Borrowing expenses	2,588,917	2,548,000
168,597	Other expenses incurred by the Crown	190,891	202,467
6,059	Other expenses - NZDMO	4,978	4,000
10,827	Depreciation	11,163	11,299
19,256	Rail assets writedowns	11,316	11,316
9,231	Change in NPF DBP(A) Scheme liability	53,151	-
(507,319)	Change in GSF unfunded liability	1,261,111	425,071
4,424	Change in valuation of Maui gas receivable	-	-
10	Other changes	27	14
46,900	Amortisation of Air New Zealand goodwill	46,900	46,900
9,612	Foreign exchange losses/(gains)	18,258	21,834
<b>3,079,033</b>		<b>5,024,357</b>	<b>4,108,781</b>
	<b>Vote Crown Research Institutes</b>		
35	Other expenses incurred by the Crown	847	1,045
<b>35</b>		<b>847</b>	<b>1,045</b>
<b>3,079,068</b>	<b>Total Non-Departmental Expenses</b>	<b>5,025,204</b>	<b>4,109,826</b>

(Figures are GST inclusive where applicable)

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# STATEMENT OF EXPENDITURE AND APPROPRIATIONS

for the year ended 30 June 2005

The Statement of Expenditure and Appropriations details expenditure and capital payments incurred against appropriations. The Department administers these appropriations on behalf of the Crown.

2004 Actual \$000		2005 Actual \$000	2005 Supp. Estimates Voted \$000
	<b>Vote Finance</b>		
	<b>Non-Departmental Output Classes</b>		
4,297	GSF Authority	4,556	4,624
3,000	Guardians of New Zealand Superannuation	4,150	4,150
3,888	Management of Auckland rail corridor	1,018	1,018
360	Management of Crown overseas properties	426	1,500
110	Management of Geothermal Trading	111	170
<b>11,655</b>		<b>10,261</b>	<b>11,462</b>
	<b>Benefits and Other Unrequited Expenses</b>		
731,428	GSFA - subsidy to Government Superannuation Fund	806,249	805,131
13,764	GSFA - subsidy to judges' superannuation account	16,336	15,758
4,349	GSFA - subsidy to parliamentary superannuation account	4,445	5,190
339	GSFA - New Zealand Superannuation Corporation annuities	354	339
(507,319)	GSF unfunded liability movement	-	-
<b>242,561</b>		<b>827,384</b>	<b>826,418</b>
	<b>Borrowing Expenses</b>		
2,549,901	Debt servicing	2,588,917	2,548,000
<b>2,549,901</b>		<b>2,588,917</b>	<b>2,548,000</b>
	<b>Other Expenses Incurred by the Crown</b>		
-	Compensation payments	-	200
6,157	Crown overseas properties	6,257	11,700
10	Crown residual liabilities	29	758
1,834	Geothermal Trading	1,684	3,330
1	Government Superannuation Appeals Board	1	50
5,783	GSF: Crown share of custodial and investment management expenses	5,945	6,438
5,688	Loss on sale of Auckland marinas	-	-
145,754	Maui gas contracts	116,859	131,000
19	Overseas Investment Commission honoraria	19	25
1,112	Establishment of Track Co	2,618	3,500
-	Upgrade of rail network	50,296	44,000
-	NZ Railways Corporation operating and maintenance costs	6,900	-
2,185	Wellington Railway Station maintenance	268	966
54	Unclaimed money	15	500
<b>168,597</b>		<b>190,891</b>	<b>202,467</b>

(Figures are GST inclusive where applicable)

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# STATEMENT OF EXPENDITURE AND APPROPRIATIONS (CONTINUED)

for the year ended 30 June 2005

2004 Actual \$000		2005 Actual \$000	2005 Supp. Estimates Voted \$000
	<b>Vote Finance (continued)</b>		
	<b>Capital Contributions to Other Organisations</b>		
-	Air New Zealand	149,350	149,350
4,600	Auckland Regional Council loan to purchase and upgrade rolling stock	10,414	20,400
110,000	International financial institutions	-	200,000
3,794,080	New Zealand Superannuation Fund	2,107,000	2,107,000
-	Reserve Bank	1,000,000	1,000,000
-	Taitokerau Forests	950	950
-	NZ Railways Corporation loans	15,000	75,000
-	Track Co working capital	20,000	20,000
93,302	Transmission Holdings Ltd	-	-
16,354	University of Auckland Business School	-	-
<b>4,018,336</b>		<b>3,302,714</b>	<b>3,572,700</b>
	<b>Purchase or Development of Capital Assets</b>		
60,464	Auckland marinas	-	-
441	Auckland rail corridor	-	-
1,996	Development of Crown overseas properties	1,554	3,100
4,339	Double tracking Auckland rail corridor	4,802	4,802
227	Geothermal Trading	3	4,273
17,647	Track Co - upgrade of Wellington Railway Station	6,924	12,416
54,978	Track Co - purchase of rail network assets	7,929	9,000
<b>140,092</b>		<b>21,212</b>	<b>33,591</b>
	<b>Repayment of Debt</b>		
681,567	Net domestic debt repayment	661,937	738,000
654,015	Net foreign debt repayment	-	-
<b>1,335,582</b>		<b>661,937</b>	<b>738,000</b>
<b>8,466,724</b>	<b>Total Vote Finance</b>	<b>7,603,316</b>	<b>7,932,638</b>
	<b>Vote Crown Research Institutes</b>		
	<b>Other Expenses Incurred by the Crown</b>		
35	CRI residual liabilities	3	200
-	CRI non-excluded liabilities	844	845
<b>35</b>	<b>Total Vote Crown Research Institutes</b>	<b>847</b>	<b>1,045</b>
<b>8,466,759</b>	<b>Total Non-Departmental Expenditure and Appropriations</b>	<b>7,604,163</b>	<b>7,933,683</b>

(Figures are GST inclusive where applicable)

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# STATEMENT OF UNAPPROPRIATED EXPENDITURE

for the year ended 30 June 2005

Vote Finance incurred two items of unappropriated expenditure during the year:

## Vote Finance, Other expenses of the Crown: New Zealand Railways Corporation operating and maintenance costs

On 20 June 2005, Cabinet approved additional funding for certain non-recoverable operating and maintenance costs of NZRC in 2004/05:

- \$3.3 million (GST inclusive) was approved to cover a shortfall between the Track Access Charge and NZRC's actual costs, and
- \$3.6 million (GST inclusive) was approved to cover the costs associated with the collapse of a bridge at Nuhaka and flooding in the Bay of Plenty.

The Minister of Finance has approved both items of unappropriated expenditure in accordance with section 12 of the Public Finance Act 1989 which, in accordance with section 33 of the Public Finance Amendment Act 2004 (PFAA), continues to apply to the year ended 30 June 2005 as if they had not been amended by the PFAA.

# SCHEDULE OF REVENUE

for the year ended 30 June 2005

2004 Actual \$000		2005 Actual \$000	2005 Supp. Estimates \$000
	<b>Vote Finance</b>		
5,343	Auckland rail corridor access fee	-	-
847	Auckland rail double tracking - grant from Infrastructure Auckland	7,278	7,278
1,091,288	Capital charge	1,119,431	1,118,722
1,062	Contact Energy Ltd Crown margin interest	2,309	1,830
7,784	Dividends from Crown entities	48,698	48,698
227,458	Dividends from SOEs	329,369	325,968
2,530	Dividends - other	2,837	2,837
10,000	Earthquake Commission guarantee fee	10,000	10,000
66,883	Employers' superannuation contributions	65,035	63,539
2	Export Credit Office	12	380
736,875	Interest from investments	769,101	658,000
20,223	Interest income - other	13,430	13,328
4,822	Other income - NZDMO	51,677	140,000
129,559	Maui gas contracts	103,875	116,000
24,755	Rentals from Crown overseas properties	23,115	25,900
184,419	Reserve Bank of New Zealand net surplus	191,747	191,747
42,851	Sale of goods and services	29,849	29,600
-	Gain on sale of assets	1,100	-
8,030	Other current revenue	13,543	871
1,590	Unclaimed money	1,744	1,500
<b>2,566,321</b>		<b>2,784,150</b>	<b>2,756,198</b>
	<b>Vote Crown Research Institutes</b>		
350	Dividends from CRIs	15,000	15,000
350		15,000	15,000
<b>2,566,671</b>	<b>Total Non-Departmental Revenue</b>	<b>2,799,150</b>	<b>2,771,198</b>

(All figures are GST exclusive)

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# SCHEDULE OF CAPITAL RECEIPTS

for the year ended 30 June 2005

The Schedule of Capital Receipts details non-departmental capital receipts that the Department administers on behalf of the Crown.

2004 Actual \$000		2005 Actual \$000	2005 Supp. Estimates \$000
	<b>Vote Finance</b>		
38,400	Contact Energy Ltd Crown margin	47,600	48,370
-	Net foreign borrowing	567,933	732,000
44,070	Loan repayments from other parties	15,084	25,070
222,000	Return of capital from the IMF	230,000	200,000
48,690	Sale of Auckland marinas	-	-
-	Sale of rail network assets to NZ Railways Corporation*	1,472	-
93,302	Transmission Holdings	-	-
<b>446,462</b>		<b>862,089</b>	<b>1,005,440</b>

(All figures are GST exclusive)

\* Certain rail network assets, purchased by the Crown from Toll Holdings, were transferred to the New Zealand Railways Corporation on 1 September 2004.

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

## SCHEDULE OF ASSETS

as at 30 June 2005

The Schedule of Assets summarises the assets that the Department administers on behalf of the Crown.

2004 Actual \$000		2005 Actual \$000	2005 Supp. Estimates \$000
1,349,305	Cash and bank accounts	715,172	1,782,562
2,823,993	Accounts receivable and advances	2,552,934	2,596,974
14,117,958	Marketable securities, deposits and equity investments	16,697,326	15,359,862
35,223	Inventory	23,045	23,133
385,290	Intangibles and goodwill	338,390	338,390
204,791	Other investments	186,075	182,720
407,339	Property, plant and equipment	426,056	410,865
<b>19,323,899</b>		<b>20,938,998</b>	<b>20,694,506</b>

(All figures are GST exclusive)

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# SCHEDULE OF LIABILITIES

as at 30 June 2005

The Schedule of Liabilities summarises the liabilities that the Department administers on behalf of the Crown.

2004 Actual \$000		2005 Actual \$000	2005 Supp. Estimates \$000
2,578,000	Overdrafts	3,317,000	2,472,000
10,168,889	GSF unfunded liability	11,430,000	10,593,960
891,020	NPF DBP(A) Scheme unfunded liability	944,171	891,020
859,314	Other payables and provisions	735,422	535,171
87,604	Coins in circulation	-	87,603
36,727,000	Borrowings	36,072,000	36,178,000
<b>51,311,827</b>		<b>52,498,593</b>	<b>50,757,754</b>

(All figures are GST exclusive)

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# SCHEDULE OF COMMITMENTS

as at 30 June 2005

30 June 2004 \$000		30 June 2005 \$000
	<b>By Type</b>	
2,019	Non-cancellable property lease	2,130
609	Other non-cancellable operating commitments	133,293
<b>2,628</b>		<b>135,423</b>
	<b>By Term</b>	
	Operating commitments	
249	Less than one year	83,223
249	One to two years	29,223
341	Two to five years	21,417
1,789	More than five years	1,560
<b>2,628</b>		<b>135,423</b>
	<b>Capital Commitments</b>	
1,500	Crown overseas properties	-
185,000	National rail network upgrades	-
5,416	Wellington Railway Station	8,525
<b>191,916</b>		<b>8,525</b>
<b>194,544</b>	<b>Total Commitments</b>	<b>143,948</b>

(All figures are GST exclusive)

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# SCHEDULE OF CONTINGENT LIABILITIES

as at 30 June 2005

30 June 2004 \$000		30 June 2005 \$000
	<b>Quantifiable Contingent Liabilities</b>	
52,232	Guarantees and indemnities	61,275
2,488,797	Uncalled capital	2,221,272
3,852	Legal proceedings and disputes	1,350
1,213,222	Other contingent liabilities	1,292,322
<b>3,758,103</b>		<b>3,576,219</b>

(All figures are GST exclusive)

Contingent liabilities are costs which the Crown will have to face if a particular event occurs. Typically, contingent liabilities consist of guarantees and indemnities, uncalled capital, legal disputes and claims. The contingent liabilities managed by the Department on behalf of the Crown are a mixture of operating and balance sheet risks and they vary greatly in magnitude and likelihood of realisation. In general, if a contingent liability were realised it would have a negative impact on the operating balance, net Crown debt and net worth. 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 included 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.

The majority of the quantified contingent liabilities shown above arise from the uncalled capital element of the Crown's investments in the Asian Development Bank and the World Bank, and promissory notes issued in favour of the IMF.

## Unquantifiable Contingent Liabilities

The Treasury also administers a number of contingent liabilities which cannot be quantified. These arise primarily from institutional guarantees and indemnities. Readers are referred to the Crown financial statements for further details.

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# STATEMENT OF TRUST MONIES

for the year ended 30 June 2005

30 June 2004 Actual \$000		30 June 2005 Actual \$000
934	Balance at the beginning of the year	912
60	Contribution	325
(1)	Distribution	(3)
48	Revenue	60
(129)	Unclaimed money returned to the Crown	(470)
912	Balance at the end of the year	824

(All figures are GST exclusive)

The Trust Account is established pursuant to section 67 of the Public Finance Act 1989 (which, in accordance with section 33 of the Public Finance Amendment Act 2004 (PFAA), continues to apply to the year ended 30 June 2005 as if they had not been amended by the PFAA), for the purposes of depositing money paid to the Crown under section 77 of the Trustee Act 1956.

The source of funds is principally estates of deceased persons where the beneficiaries cannot be traced. Funds are retained in the Trust Account for six years, and are then transferred to the Crown as unclaimed money. During the financial year ended 30 June 2005, \$3,000 was paid to claimants and interest of \$60,000 was earned from trust money on term deposit.

Details of funds held in the Trust Account are gazetted annually.

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# NEW ZEALAND DEBT MANAGEMENT OFFICE

for the year ended 30 June 2005

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NZDMO is an operating unit of the Treasury. NZDMO is responsible for managing the Crown's debt, overall cashflows and interest-bearing deposits. To facilitate a greater level of transparency regarding NZDMO operations as distinct from other entities, a separate section on NZDMO is provided in the Treasury Annual Report.

The following supplementary financial schedules reflect the activity of NZDMO as though it were a stand-alone entity. Cross-holdings or other financial positions between NZDMO and other government entities are not eliminated.

NZDMO managed \$13,641 million of assets, \$40,083 million of liabilities, \$825 million of revenue and \$2,594 million of expenses on behalf of the Crown for the year ended 30 June 2005.

Further information on NZDMO's performance in managing the Crown's sovereign-issued debt and related financial assets is provided in the Debt and Related Financial Asset Management output performance section of this report on pages 60 to 61. NZDMO's contribution to the "efficient management of the Crown's assets and liabilities" outcome is discussed on pages 21 to 25 of this report.

The financial information reported in these schedules is consolidated into the Crown financial statements. Readers should refer to the Crown financial statements for the year ended 30 June 2005.

## NATURE AND EXTENT OF ACTIVITIES

NZDMO, established in 1988, is part of the New Zealand Treasury and is responsible for the efficient management of the Crown's debt and associated assets within an appropriate risk management framework. NZDMO's strategic objective is to maximise the long-term economic return on the Crown's financial assets and debt in the context of the Government's fiscal strategy, particularly its aversion to risk. NZDMO's major responsibilities involve:

- financing the Crown's gross borrowing requirement, managing foreign-currency assets required to meet net foreign-currency interest and principal payments, and settling and accounting for all related debt transactions
- maintaining and developing an appropriate framework for efficiently managing the portfolio and the risks associated with it
- disbursing cash to departments and facilitating departmental cash management
- advancing funds to government entities in accordance with Government policy
- providing capital markets services and derivative transactions for departments and government entities
- providing reporting for fiscal forecasting and financial statements
- maintaining a diversified funding base and, where appropriate, enhancing relationships with investors who hold, or are potential holders of, New Zealand government securities and with financial intermediaries and the international credit rating agencies.



NZDMO's Accounting and Transactional Services team – Ross Jamieson, Heidi Pieterse, Neil Bain, Susanna Vandenberg and Jane Alexander

# SCHEDULE OF ASSETS AND LIABILITIES

as at 30 June 2005

The Schedule of Assets and Liabilities summarises the assets and liabilities managed by NZDMO.

Book Value 2004 \$m	Fair Value 2004 \$m		Book Value 2005 \$m	Fair Value 2005 \$m
		<b>Foreign Currency Assets</b>		
2,576	2,589	Marketable securities	4,865	4,873
335	335	External deposits	533	533
3,842	3,842	Advances to Reserve Bank of New Zealand (RBNZ)	3,940	3,940
(1,655)	(1,505)	Derivatives <sup>1</sup>	(218)	(54)
916	916	IMF reserve position	609	609
254	254	Debtors and receivables	67	67
11	11	Foreign bank accounts	6	6
<b>6,279</b>	<b>6,442</b>		<b>9,802</b>	<b>9,974</b>
		<b>New Zealand Dollar Assets</b>		
1,242	1,242	Crown settlement account	667	667
861	858	Advances to Crown Financing Agency	814	810
1,259	1,259	Advances to Housing New Zealand	1,299	1,299
2,202	2,198	Derivatives <sup>1</sup>	923	935
53	53	Debtors and receivables <sup>2</sup>	69	69
53	80	Other	67	97
<b>5,670</b>	<b>5,690</b>		<b>3,839</b>	<b>3,877</b>
<b>11,949</b>	<b>12,132</b>	<b>Total Assets</b>	<b>13,641</b>	<b>13,851</b>
		<b>Foreign Currency Liabilities</b>		
4,049	4,269	Debt	2,995	3,185
1,763	1,814	Derivatives <sup>1</sup>	6,685	6,569
293	293	Creditors and payables <sup>2</sup>	219	219
<b>6,105</b>	<b>6,376</b>		<b>9,899</b>	<b>9,973</b>
		<b>New Zealand Dollar Liabilities</b>		
5,701	5,694	Treasury bills	5,466	5,469
24,333	24,595	Government bonds <sup>3</sup>	25,024	25,678
1,678	1,898	Inflation-indexed bonds	1,730	2,032
441	440	Kiwi bonds	416	416
2,578	2,578	Crown balances with Westpac <sup>4</sup>	3,317	3,317
(1,262)	(1,204)	Derivatives <sup>1</sup>	(6,262)	(6,120)
483	483	Creditors and payables	475	475
24	29	Other	18	19
<b>33,976</b>	<b>34,513</b>		<b>30,184</b>	<b>31,286</b>
<b>40,081</b>	<b>40,889</b>	<b>Total Liabilities</b>	<b>40,083</b>	<b>41,259</b>

1 Each derivative transaction is recorded as an asset or a liability based on its year-end value.

2 Accrued interest, including on derivatives, is recognised under payables or receivables.

3 Government bonds include non-market issues to the Reserve Bank of New Zealand.

4 Crown balances with Westpac at 30 June 2005 include the NZDMO Disbursement account (\$3.547 million O/D). NZDMO disburses funds from this account to bank accounts maintained by departments and the account operates as an effective contra to the balances held by departments.

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

# SCHEDULE OF REVENUES AND EXPENSES

for the year ending 30 June 2005

The Schedule of Revenues and Expenses summarises the revenues and expenses associated with the assets and liabilities managed by NZDMO.

2004 \$m		2005 \$m
	<b>Foreign Currency Revenue</b>	
60	Marketable securities	95
6	External deposits	12
103	Advances to RBNZ	108
246	Derivatives	327
13	IMF reserve position	12
(69)	Unrealised gains/losses on advances to RBNZ	(84)
<b>359</b>		<b>470</b>
	<b>New Zealand Dollar Revenue</b>	
179	Crown settlement account	77
23	Advances to Crown Financing Agency	51
51	Advances to Housing New Zealand	85
130	Derivatives	138
5	Other	4
<b>388</b>		<b>355</b>
<b>747</b>	<b>Total Revenue</b>	<b>825</b>
	<b>Foreign Currency Expenses</b>	
194	Debt	169
100	Derivatives	72
3	Foreign exchange gains/losses	8
4	Other	(3)
<b>301</b>		<b>246</b>
	<b>New Zealand Dollar Expenses</b>	
343	Treasury bills	338
1,710	Government bonds	1,654
112	Inflation-indexed bonds	134
24	Kiwi bonds	23
51	Derivatives	183
15	Other	16
<b>2,255</b>		<b>2,348</b>
<b>2,556</b>	<b>Total Expenses</b>	<b>2,594</b>

*The Crown's accounting policies are an integral part of these supplementary financial schedules.*

## Risk management

With ministerial approval, NZDMO maintains a portfolio and risk management framework within which it operates. That includes NZDMO's strategic objective, objectives for New Zealand-dollar and foreign-currency debt, the instruments in which NZDMO may transact, limits in respect of market and credit risk utilisation, composition requirements for the liquidity asset portfolio and maturity profile requirements.

The risk management framework has been in place since NZDMO was established. The specifics of implementation have been subject to continuous improvement as resources allow and as information technology capability and analytical techniques have improved. Careful prioritisation ensures that resources are allocated to managing the most significant risks first and that fundamental risks are covered. In addition, NZDMO periodically commissions reviews by external experts of its risk management framework and practices, including the strategic parameters of the portfolio.

The basis of operation is well defined, including the legal authority to borrow and service debt and NZDMO's internal organisation. Internal operations are managed through an established risk culture, body of policies, ethical guidelines and codes of conduct, defined responsibilities and accountabilities, formal delegations, segregated duties, limits, reporting and performance management requirements, procedural manuals and established processes.

## Credit risk

Credit risk refers to the risk of a counterparty failing to discharge an obligation.

Credit losses arise when NZDMO is required to find a transaction counterparty to replace one that is no longer of acceptable credit quality. In finding a suitable replacement, NZDMO would incur transaction costs and potentially suffer a loss in the market value of the original transaction. Credit losses also arise when the issuer of a financial obligation that NZDMO holds as an asset is downgraded or defaults.

Financial instruments that subject NZDMO to credit risk include bank balances, advances, investments, interest-rate swaps, currency swaps, and foreign-exchange forward contracts.

NZDMO manages credit risk through the use of credit exposure limits. Credit exposures are maintained only with highly rated institutions for which the probability of default is low. To diversify credit exposure, NZDMO limits its exposure to any one institution. The creditworthiness of counterparties is continuously monitored. Credit risk is further controlled by incorporating credit support annexes into master swap agreements with swap and foreign exchange counterparties. Credit risk is measured using an in-house credit model that conforms to industry best practice.

As at 30 June 2005, total credit exposure was calculated as follows:

2004 \$m		2005 \$m
11,949	Total NZDMO assets	13,641
	Less	
7,207	Crown-related balances	6,766
78	Crown-related derivatives	129
308	Receivables	137
<b>4,356</b>	<b>Total Credit Exposure</b>	<b>6,609</b>
	Comprising	
11	Foreign bank accounts	6
50	Advances	50
335	External deposits	533
2,576	Marketable securities	4,836
468	Derivatives	575
916	IMF	609
<b>4,356</b>		<b>6,609</b>

As at 30 June 2005, concentrations of credit exposure by industry type were as follows:

2004 \$m		2005 \$m
407	Sovereign issuers	2,514
1,063	Supranationals	1,147
2,473	Banks	2,158
413	Other	790
<b>4,356</b>	<b>Total Credit Exposure</b>	<b>6,609</b>

As at 30 June 2005, concentrations of credit exposure by geographical area were as follows:

2004 \$m		2005 \$m
771	United States	1,056
1,737	Europe	3,505
26	Japan	24
462	Australia	436
284	New Zealand	366
1,063	Supranationals	1,147
13	Other	75
<b>4,356</b>	<b>Total Credit Exposure</b>	<b>6,609</b>

As at 30 June 2005, concentrations of credit exposure by credit rating were as follows:

2004 \$m		2005 \$m
1,339	AAA	4,458
1,857	AA	1,350
244	A	192
916	IMF reserve position	609
<b>4,356</b>	<b>Total Credit Exposure</b>	<b>6,609</b>

## Collateral

For swaps and foreign-exchange contracts transacted under NZDMO's customised International Swaps and Derivatives Association (ISDA) swap documentation, collateral is required when the mark-to-market exposure exceeds the credit exposure limit for a counterparty.

As at 30 June 2005, NZDMO held the following as collateral against counterparties under credit support annexes to master swap agreements:

2004 \$m	2005 \$m
213 Cash deposits	423
- US Treasury bills	-
<b>213 Total Collateral Held</b>	<b>423</b>

## Settlement exposure

The settlements process involves the receipt and payment of funds and securities, and default by a settlement agent would result in NZDMO being unable to make or receive payments with that agent.

The nature of NZDMO's business is such that large amounts may be settled on one day. For that reason, monetary limits are not placed on NZDMO's exposure to transaction banks, custodians, fiscal agents and clearing brokers. Risk in respect of those institutions is managed through procedures for selecting and monitoring transaction settlement agents.

## Interest-rate and foreign-exchange risk

Interest-rate risk refers to the risk of loss due to adverse movement in interest rates. Foreign-exchange risk refers to the risk of loss due to adverse movements in foreign-exchange rates.

### New Zealand-dollar assets and liabilities

The New Zealand-dollar portfolio is driven by a set of principles that support NZDMO's debt management objective, rather than one strategic benchmark. These principles are used to manage the risks and costs of the New Zealand-dollar portfolio and help NZDMO issue debt cost effectively. The market value of New Zealand-dollar debt is not actively managed.

In general, interest-rate risk is managed strategically. To diversify interest-rate risk and lower the cost of the portfolio, NZDMO maintains a mix of fixed-rate and floating-rate debt and uses interest-rate swaps. Inflation-indexed debt makes up a component of the portfolio and has been issued when it was cost effective to do so. Bonds are issued into benchmark lines to improve liquidity in the market and, consequently, reduce the Crown's cost of borrowing. When issuing domestic securities, NZDMO samples interest rates throughout the year by conducting monthly auctions of Government bonds and weekly auctions of Treasury bills. NZDMO is committed to transparency, predictability and even-handedness in its domestic securities' issuance.

### Foreign currency assets and liabilities

NZDMO manages interest rate and foreign exchange risk in the foreign-currency portfolio in an integrated manner.

Unless otherwise directed by the Minister of Finance, NZDMO's net foreign-currency debt position is kept close to zero when measured on a market value basis. With ministerial approval, there are specified conservative position and loss limits that allow some discretionary trading to take place. Market risk is incurred from that discretionary activity due to movements in interest rates and foreign-exchange rates. The range of

instruments used to minimise exposure to market risk includes foreign-exchange contracts, currency swaps, interest-rate swaps and futures contracts.

Market risk associated with discretionary trading is managed through the use of value at risk (VAR) limits and stop-loss limits. A VAR limit is maintained for the overall foreign-currency portfolio. It is expressed over daily, monthly and annual time horizons at a 95% confidence level and reflects the risk tolerance of the Government in respect of discretionary activity undertaken by NZDMO.

A stop-loss limit is in place to protect NZDMO from further losses once actual losses reach a certain point. It reflects the tolerance of the Government in respect of maximum acceptable losses over monthly, quarterly and annual time horizons.

NZDMO uses back-testing to evaluate the performance of the VAR model. Actual profit and loss are compared with the market risk estimates calculated using the VAR model to determine its integrity and performance. Consistent with industry best practice, VAR is supplemented with stress-testing to understand how extreme or unusual events would impact on the portfolio.

## Refinancing and repricing risk

Refinancing and repricing risk refers to the risk that maturing debt is refinanced, maturing assets are reinvested or instruments repriced at an unacceptable yield.

To manage the refinancing risk associated with New Zealand-dollar borrowing, NZDMO establishes a relatively even maturity profile for debt across the yield curve to manage the funding requirement, and the uncertainty around it arising from fiscal shocks, flexibly and without putting undue pressure on interest rates. In respect of foreign-currency borrowing, NZDMO establishes a maturity profile for debt that reduces the likelihood of being unable to access markets in a timely manner or raise funds at an acceptable cost.

Repricing risk is further diversified through the use of interest-rate swaps.

As at 30 June 2005, assets and liabilities will mature or reprice within the following periods:

	2005 \$m	0-12 Months \$m	1-2 Years \$m	2-5 Years \$m	5-10 Years \$m	>10 Years \$m
<b>Foreign Currency Assets</b>						
Marketable securities	5,474	5,062	177	172	63	-
External deposits	533	533	-	-	-	-
Advances to RBNZ	3,940	3,453	453	34	-	-
Derivatives	(218)	(1,506)	430	294	344	220
Debtors and receivables	67	67	-	-	-	-
Foreign bank accounts	6	6	-	-	-	-
	<b>9,802</b>	<b>7,615</b>	<b>1,060</b>	<b>500</b>	<b>407</b>	<b>220</b>
<b>New Zealand Dollar Assets</b>						
Crown settlement account	667	667	-	-	-	-
Advances to Crown Financing Agency	814	473	148	193	-	-
Advances to Housing New Zealand	1,299	1,249	-	50	-	-
Derivatives	923	(2,541)	289	1,194	1,981	-
Debtors and receivables	69	69	-	-	-	-
Other	67	49	-	3	15	-
	<b>3,839</b>	<b>(34)</b>	<b>437</b>	<b>1,440</b>	<b>1,996</b>	<b>-</b>
<b>Total Assets</b>	<b>13,641</b>	<b>7,581</b>	<b>1,497</b>	<b>1,940</b>	<b>2,403</b>	<b>220</b>
<b>Foreign Currency Liabilities</b>						
Debt	2,995	1,367	340	661	471	156
Derivatives	6,685	5,947	827	(87)	(65)	63
Creditors and payables	219	219	-	-	-	-
	<b>9,899</b>	<b>7,533</b>	<b>1,167</b>	<b>574</b>	<b>406</b>	<b>219</b>
<b>New Zealand Dollar Liabilities</b>						
Treasury bills	5,466	5,466	-	-	-	-
Government bonds	25,024	3,657	3,632	5,914	11,430	391
Inflation-indexed bonds	1,730	-	-	-	-	1,730
Kiwi bonds	416	310	68	38	-	-
Crown balances with Westpac	3,317	3,317	-	-	-	-
Derivatives	(6,262)	(4,343)	(240)	(708)	(771)	(200)
Creditors and payables	475	475	-	-	-	-
Other	18	12	1	3	1	1
	<b>30,184</b>	<b>8,894</b>	<b>3,461</b>	<b>5,247</b>	<b>10,660</b>	<b>1,922</b>
<b>Total Liabilities</b>	<b>40,083</b>	<b>16,427</b>	<b>4,628</b>	<b>5,821</b>	<b>11,066</b>	<b>2,141</b>

- 1 The figures reported above, including derivatives, are exclusive of accrued interest. Derivative values will differ from the book values reported in the "Derivatives" table where accrued interest is included.
- 2 Derivatives may contribute to two different repricing buckets. Floating legs would reprice within 12 months while the fixed leg would be classified according to swap maturity.

## Liquidity risk

Liquidity risk refers to the risk of loss due to the lack of market liquidity preventing timely or cost-effective liquidation of products, positions or portfolios. To manage liquidity risk, NZDMO holds readily liquefiable assets in sufficient quantity to cover off all obligations falling due over rolling six-week and 12-week horizons.

## Derivatives

NZDMO's involvement in derivatives comprises foreign-exchange contracts, currency swaps, interest-rate swaps and futures contracts.

As at 30 June 2005, the value of derivatives\* was as follows:

Book Value 2004 \$m	Fair Value 2004 \$m		Book Value 2005 \$m	Fair Value 2005 \$m
<b>Foreign-Exchange Contracts</b>				
102	95	In gain position	182	175
(84)	(85)	In loss position	(136)	(135)
<b>18</b>	<b>10</b>	<b>Net Position</b>	<b>46</b>	<b>40</b>
<b>Currency Swaps</b>				
330	349	In gain position	413	469
(409)	(399)	In loss position	(258)	(262)
<b>(79)</b>	<b>(50)</b>	<b>Net Position</b>	<b>155</b>	<b>207</b>
<b>Interest-Rate Swaps</b>				
169	332	In gain position	137	322
(15)	(162)	In loss position	(21)	(102)
<b>154</b>	<b>170</b>	<b>Net Position</b>	<b>116</b>	<b>220</b>
<b>Futures</b>				
3	3	In gain position	2	2
-	-	In loss position	0	0
<b>3</b>	<b>3</b>	<b>Net Position</b>	<b>2</b>	<b>2</b>

\* Derivatives' positions include accrued interest.

As at 30 June 2005, the notional value of derivatives was as follows:

Notional Value 2004 \$m		Notional Value 2005 \$m
7,688	Foreign-exchange contracts	13,062
4,560	Currency swaps	5,143
6,551	Interest-rate swaps	6,776
1,186	Futures	625

## Operational risk

Operational risk refers to the risk of loss due to an event that could impact on NZDMO's ability to produce its outputs to the quality, quantity and cost specified. Risk events include resource failures or constraints, control and security breaches or failures, transaction errors, compliance breaches, poor strategic decisions, the breakdown of key relationships and disasters.

Operational risks are managed in a number of ways. Operational risk policies span, for instance, transaction processing, legal and regulatory issues, ethical standards, physical and systems security, and business continuity. Independent experts, such as external auditors, provide additional support in managing operational risk. NZDMO managers assess the organisation's operational risk profile annually.

# AUDIT REPORT



## Report of the Auditor-General

### To the Readers of the Financial Statements of the Treasury For the year ended 30 June 2005

The Auditor-General is the auditor of the Treasury (the Department). The Auditor-General has appointed me, Andrew Dinsdale, using the staff and resources of KPMG, to carry out the audit of the financial statements of the Department, on his behalf, for the year ended 30 June 2005.

#### Unqualified opinion

In our opinion the financial statements of the Department on pages 49 to 72, pages 81 to 86 and 92 to 106, and the supplementary schedules on pages 110 to 120 and 123 to 130:

- comply with generally accepted accounting practice in New Zealand, and
- fairly reflect:
  - the Department's financial position as at 30 June 2005
  - the results of its operations and cash flows for the year ended on that date
  - its service performance achievements measured against the performance targets adopted for the year ended on that date, and
  - the assets, liabilities, revenues, expenses, contingencies, commitments and trust monies managed by the Department on behalf of the Crown for the year ended 30 June 2005.

The audit was completed on 21 September 2005, and is the date at which our opinion is expressed.

The basis of the opinion is explained below. In addition, we outline the responsibilities of the Chief Executive and the Auditor, and explain our independence.

#### Basis of opinion

We carried out the audit in accordance with the Auditor-General's Auditing Standards, which incorporate the New Zealand Auditing Standards.

We planned and performed our audit to obtain all the information and explanations we considered necessary in order to obtain reasonable assurance that the financial statements did not have material misstatements, whether caused by fraud or error.

Material misstatements are differences or omissions of amounts and disclosures that would affect a reader's overall understanding of the financial statements. If we had found material misstatements that were not corrected, we would have referred to them in the opinion.

The audit involved performing procedures to test the information presented in the financial statements. We assessed the results of those procedures in forming our opinion.

Audit procedures generally include:

- determining whether significant financial and management controls are working and can be relied on to produce complete and accurate data
- verifying samples of transactions and account balances
- performing analyses to identify anomalies in the reported data
- reviewing significant estimates and judgements made by the Secretary to the Treasury
- confirming year-end balances
- determining whether accounting policies are appropriate and consistently applied, and
- determining whether all financial statement disclosures are adequate.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements.

We evaluated the overall adequacy of the presentation of information in the financial statements. We obtained all the information and explanations we required to support the opinion above.

### Responsibilities of the Chief Executive and the Auditor

The Secretary to the Treasury is responsible for preparing financial statements in accordance with generally accepted accounting practice in New Zealand. Those financial statements must fairly reflect the financial position of the Department as at 30 June 2005. They must also fairly reflect the results of its operations and cash flows and service performance achievements for the year ended on that date. In addition, they must fairly reflect the assets, liabilities, revenues, expenses, contingencies, commitments and trust monies managed by the Department on behalf of the Crown for the year ended 30 June 2005. The Secretary to the Treasury's responsibilities arise from the Public Finance Act 1989.

We are responsible for expressing an independent opinion on the financial statements and reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001 and section 38(1) of the Public Finance Act 1989.

### Independence

When carrying out the audit we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the Institute of Chartered Accountants of New Zealand.

In addition to the audit we have carried out assignments in the areas of general accounting and risk management advice and assistance with the implementation of New Zealand International Financial Reporting Standards for the Crown, which are compatible with the independence requirements. Other than the audit and these assignments, we have no relationship with or interests in the Department.



Andrew Dinsdale

KPMG

On behalf of the Auditor-General

Wellington, New Zealand

# QUALITY STANDARDS FOR ANALYSIS AND ADVICE

Quality Characteristic	Description
Purpose	The objective for the advice is clearly stated, it answers any financial and economic issues raised by the Minister and demonstrates a clear understanding of the desired outcome(s) of the Government and/or the Minister.
Problem definition	Any public policy problem, including the underlying causes, size and materiality of issues, is identified and supported by data or other evidence.
Context	It is clear where the advice stands in the context of the wider policy process, including what has already been undertaken and what is expected to occur in the future. CCMAU's advice is undertaken in the context of the Government's ownership expectations for SOEs and/or CRIs.
Logic	An appropriate analytical framework is used. Assumptions behind the advice are explicit and the argument is logical and supported by facts.
Accuracy	All material facts are present and accurate. Known gaps that could significantly affect the conclusions are identified and the range of uncertainty stated. Forecasts are credible at the time they are produced and take into account all relevant information.
Options	A range of options is presented that provides clearly differentiated choices and these are rigorously evaluated against the analytical framework. Costs, benefits, consequences and risks/opportunities of the options are assessed as part of the analysis. Where it is not appropriate to use a range of options the reasons are clearly stated.
Recommendations	Recommendations are clear, logical and action oriented and can stand alone from the rest of the advice. They are sufficient to enable a decision to be made on the proposal or to move to the next decision/action point.
Consultation	Evidence of thorough and timely consultation with other government departments and interested parties is presented, and their views, including objections, incorporated as appropriate.
Practicality	Issues of implementation, technical feasibility, practicality and timing are considered and advice accurately identifies compliance, transitional, political, legislative, revenue, expense and administrative implications and costs (quantified where possible).
Communication	Guidance is provided on how communications arising from decisions on the advice should be handled, including an assessment of key stakeholders who should be informed and how.
Presentation	Material is presented to suit the target audience and: <ul style="list-style-type: none"> <li>• is concise and structured in a way which assists others to understand the aim of the advice, key features of the information, analysis and recommendations, and their key implications</li> <li>• uses appropriate language and style</li> <li>• uses empirical evidence</li> <li>• avoids clichés and technical jargon (or where the latter is not possible, is used appropriately for a general audience)</li> <li>• is consistent with departmental and Cabinet Office presentation requirements.</li> </ul>

Note: All aspects of the standards may not apply to specific pieces of policy advice, given considerations of urgency or the particular nature of the advice to be provided. For instance, much of our work is second-opinion advice on other departments' proposals often undertaken under tight time pressures.

# LEGISLATION

as at 30 June 2005

**Budget legislation administered by the Treasury during the year:**

Appropriation Act(s)  
Imprest Supply Act(s)

**Other legislation administered by the Treasury:**

Bank of New Zealand Act 1988  
Crown Entities Act 2004 (Part 4)  
Crown Forest Assets Act 1989  
Crown Research Institutes Act 1992  
Export Guarantee Act 1964  
Farm and Fishing Vessel Ownership Savings Schemes (Closure) Act 1998  
Finance Acts (Various)  
Government Superannuation Fund Act 1956  
Hawkes Bay Earthquake Act 1931  
Institute of Chartered Accountants of New Zealand Act 1996  
International Finance Agreements Act 1961  
National Expenditure Adjustment Act 1932  
National Provident Fund Restructuring Act 1990  
National Savings Act 1940  
New Zealand Government Property Corporation Act 1953  
New Zealand Railways Corporation Restructuring Act 1990  
New Zealand Railways Staff Welfare Society Dissolution Act 1999  
New Zealand Superannuation Act 2001 (various provisions)  
Post Office Bank Act 1987  
Public Audit Act 2001  
Public Finance Act 1989  
Radio New Zealand Act 1995  
Radio New Zealand Act (No 2) 1995  
Rural Banking and Finance Corporation of New Zealand Act 1989  
Southland Electricity Act 1993  
State Insurance Act 1990  
State-Owned Enterprises Act 1986  
Superannuation Schemes Act 1989  
Tourist Hotel Corporation of New Zealand Act 1989  
Treasurer (Statutory References) Act 1997

**Delegated legislation administered by the Treasury:**

Bank of New Zealand Order 1989  
Crown Entities (Financial Powers) Regulations 2005  
Crown Research Institutes Act Commencement Order 1998  
Electricity Industry Reform Act Commencement Orders (various)  
Export Guarantee Amendment Act Commencement Order 1990  
Finance Acts Orders (various)  
International Finance Agreements Amendment Act Commencement Order 1978  
National Provident Fund (Approval of Amendments to Restructuring Proposal) Order 1993  
National Savings Investment Account Regulations (various)  
New Zealand Railways Corporation Restructuring Act Orders (various)  
New Zealand Railways Staff Welfare Society Dissolution Act Commencement Order 1999  
Post Office Bank Amendment Act Orders (various)  
Public Audit (West Coast Development Trust) Order 2002  
Public Finance Act Orders (various)  
Radio New Zealand Orders (various)  
Southland Electricity Act Commencement Order 1994  
State Insurance Act (Vesting) Order 1990  
State-Owned Enterprises Act Orders (various)  
Tourist Hotel Corporation of New Zealand Act Commencement Order 1990  
Tower Corporation Act Commencement Order 1990

# WORKING AND POLICY PERSPECTIVES PAPERS

for the year ended 30 June 2005

The Treasury working and policy perspectives papers contain work in progress on a variety of economic, financial, trade and social issues.

Our aim in publishing is to make papers available to a wider audience, and to inform and encourage public debate. They are an electronic publication that can be viewed on our website:

[www.treasury.govt.nz/workingpapers](http://www.treasury.govt.nz/workingpapers)

Papers added during 2004/05 include:

## Policy Perspectives Papers

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### 2005

- 05/03 Pricing in Wholesale Electricity Markets by Sharron Came and Max Dupuy
- 05/02 Central Government Guidance and the Resource Management Act by Kevin Guerin
- 05/01 Population Ageing and Government Health Expenditures by John Bryant, Audrey Sonerson, Martin Tobias, Jit Cheung and Mhairi McHugh

## Working Papers

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### 2005

- 05/07 The Changing Gender Distribution of Paid and Unpaid Work in New Zealand by Paul Callister
- 05/06 Women's Participation in the Labour Force by Grant Johnston
- 05/05 Capital Shallowness: A Problem for New Zealand? by Julia Hall and Grant Scobie
- 05/04 Returns to Scale, Technical Progress and Total Factor Productivity Growth in New Zealand Industries by Kevin J Fox
- 05/03 The Living Standards, Incomes and Accommodation Costs of Older New Zealanders Revisited by Roger Hurnard, Dean Hyslop and Ivan Tuckwell
- 05/02 Taxes vs. Permits: Options for Price-Based Climate Change Regulation by Suzi Kerr, Isabelle Sin and Joanna Hendy
- 05/01 The Contributions from Firm Entry, Exit and Continuation to Labour Productivity Growth in New Zealand by David Law and Nathan McLellan

### 2004

- 04/25 Carbon Dioxide Emissions Reductions in New Zealand: A Minimum Disruption Approach by John Creedy and Catherine Sleeman
- 04/24 Adult Literacy and Economic Growth by Grant Johnston
- 04/23 Carbon Taxation, Prices and Household Welfare in New Zealand by John Creedy and Catherine Sleeman
- 04/22 Women's Retirement Incomes in New Zealand: A Household Bargaining Approach by John Gibson, Trinh Le and Grant Scobie
- 04/21 Adult Equivalence Scales, Inequality and Poverty in New Zealand by John Creedy and Catherine Sleeman
- 04/20 Household Incomes in New Zealand: The Impact of the Market, Taxes and Government Spending, 1987/88-1997/98 by Ron Crawford and Grant Johnston
- 04/19 Institutions, Firms and Economic Growth by Jane Frances
- 04/18 Trade and Migration to New Zealand by John Bryant, Murat Genc and David Law
- 04/17 Financial Systems and Economic Growth: An Evaluation Framework for Policy by Iris Claus, Veronica Jacobsen and Brock Jera
- 04/16 Workplace Skills, Technology Adoption and Firm Productivity: A Review by Sid Durbin
- 04/15 "Managing for Outcomes" in the New Zealand Public Management System by Anna-Luis Cook
- 04/14 Population Ageing and Government Health Expenditures in New Zealand, 1951-2051 by John Bryant, Audrey Teasdale, Martin Tobias, Jit Cheung and Mhairi McHugh
- 04/13 New Zealand's Diaspora and Overseas-born Population by John Bryant and David Law
- 04/12 Saving for Retirement: New Evidence for New Zealand by Grant Scobie, John Gibson and Trinh Le
- 04/11 Firm Dynamics in New Zealand: A Comparative Analysis with OECD Countries by Duncan Mills and Jason Timmins
- 04/10 Estimating a New Zealand NAIRU by Kam Leong Szeto and Melody Guy