

Fiscal Risks

Introduction

This chapter describes the fiscal risks to the Government, including specific fiscal risks, and contingent liabilities, and notes charges against the fiscal forecasts.

Legislative Requirements

The Public Finance Act 1989 (PFA) requires an Economic and Fiscal Update to incorporate, to the fullest extent possible consistent with the limits on disclosure requirements set out below, all government decisions and other circumstances that may have a material effect on the fiscal and economic outlook. If the fiscal implications of government decisions and other circumstances can be quantified for particular years with reasonable certainty, these fiscal implications must be included in the forecast financial statements. If the fiscal implications of government decisions and other circumstances cannot be quantified for particular years with reasonable certainty, those government decisions or other circumstances must be disclosed in the statement of specific fiscal risks.

The PFA requires the Minister of Finance and the Secretary to the Treasury to sign a statement of responsibility for each Economic and Fiscal Update that:

- the Minister of Finance has communicated to the Secretary to the Treasury before the Economic and Fiscal Update is finalised, all policy decisions with material economic or fiscal implications that the Government has made, and all other circumstances with material economic or fiscal implications of which the Minister is aware, and
- the Secretary to the Treasury has incorporated in the Economic and Fiscal Update the fiscal and economic implications of those decisions and other circumstances, using the Treasury's best professional judgement (on the basis of the economic and fiscal information available to the Treasury on the day before the Economic and Fiscal Update was finalised).

The PFA also requires the statement of specific fiscal risks of the Government to disclose the rules used to determine what is and what is not a specific fiscal risk.

The PFA requires that the fiscal forecasts must be prepared in accordance with generally accepted accounting practice (GAAP).

FRS-42 *Prospective Financial Statements* provides GAAP guidance for preparing fiscal forecasts. The general principle of the standard is that forecasts should be prepared using the best information that is reasonable and supportable. To ensure the accuracy of the fiscal forecasts the forecast assumptions:

- are based on the best information that is available at the time the forecasts are prepared (eg, latest economic conditions)
- are consistent with the current plans of the Government (eg, include current policies and other policies the Government is considering), and
- have a reasonable and supportable basis (eg, events are probable and measurable).

There will always be an element of judgement surrounding the assumptions that are made in preparing the fiscal forecasts. To provide a more comprehensive picture of the fiscal position FRS-42 also requires disclosure of factors that may lead to a material difference between the forecasts and the actual results. This includes matters such as new policies the Government may be considering and sensitivity around key assumptions (eg, economic conditions).

Criteria and Rules for Disclosure in the Fiscal Forecasts or as Specific Fiscal Risks

All government decisions and other circumstances that may have a material effect on the fiscal and economic outlook are considered against the criteria and rules set out below to determine if they are to be incorporated into the fiscal forecasts, disclosed as specific fiscal risks or, in some circumstances, excluded from disclosure.

Criteria for including matters in the fiscal forecasts

Matters are incorporated into the fiscal forecasts provided they meet all of the following criteria:

- The quantum is more than \$10 million in any one year.
- The matter can be quantified for particular years with reasonable certainty.
- A decision has been taken; or a decision has not yet been taken, but it is reasonably probable⁷ the matter will be approved, or it is reasonably probable the situation will occur.

Additionally, any other matters may be incorporated into the forecasts if the Secretary to the Treasury considers, using his or her best professional judgement, that the matters may have a material effect on the fiscal and economic outlook and are certain enough to include in the fiscal forecasts.

⁷ For these purposes “reasonably probable” is taken to mean that the matter is more likely than not to be approved within the forecast period (by considering, for example, whether there is a better than 50% chance of the matter occurring or being approved).

Rules for the disclosure of specific fiscal risks

Matters are disclosed as specific fiscal risks if:

- the likely cost is more than \$10 million in any one year, and either
- a decision has not yet been taken, but it is reasonably possible⁸ (but not probable) that the matter will be approved or the situation will occur, or
- it is reasonably probable that the matter will be approved or the situation will occur, but the matter cannot be quantified for or assigned to particular years with reasonable certainty.

Additionally, any other matters may be disclosed as specific fiscal risks if the Secretary to the Treasury considers, using his or her best professional judgement, that the matters may have a material effect (more than \$10 million in any one year) on the fiscal and economic outlook, but are not certain enough to include in the fiscal forecasts.

Exclusions from disclosure

Matters are excluded from disclosure as specific fiscal risks if they fail to meet the materiality criteria (ie, are less than \$10 million in every year), or if it is unlikely⁹ they will be approved or occur within the forecasting period.

Additionally, the Minister of Finance may determine that an item included in the fiscal forecasts or a specific fiscal risk not be disclosed, if such disclosure would be likely to:

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

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

⁸ For these purposes “reasonably possible” is taken to mean that the matter might be approved within the forecast period (by considering, for example, whether there is a 20% to 50% chance of the matter occurring or being approved).

⁹ For these purposes “unlikely” is taken to mean that the matter will probably not be approved within the forecast period (by considering, for example, whether there is a less than 20% chance of the matter occurring or being approved).

Information Relating to all Disclosed Risks

Allowances for additional operating and capital spending in future Budgets are incorporated into the fiscal forecasts. From Budget 2011 the operating allowance is set at \$1.12 billion per Budget (grown forward at 2% per annum) and the capital allowance is \$1.39 billion per Budget from 2011 to 2014.

The risks outlined in this chapter, should they eventuate, would only have an effect on the operating balance and/or net debt to the extent that they were not funded from within the allowances, by reprioritising existing expenditure or through third-party revenue.

Policy options for many risks require further development, and the quantum of the risk is often uncertain. Consequently, the final cost or saving may differ from the amounts disclosed in this chapter.

Charges Against the Fiscal Forecasts

The PFA requires that if the fiscal implications of government decisions and other circumstances can be quantified for particular years with reasonable certainty, these fiscal implications must be included in the forecast financial statements. This applies irrespective of whether or not a decision has been taken by the Government to provide additional funding for the matter.

Based on the criteria outlined in pages 86 and 87, none of the risks outlined in this chapter are considered probable enough to be included as charges against the fiscal forecasts.

Specific Fiscal Risks

The matters listed below are disclosed as specific fiscal risks as they meet the rules for disclosure outlined on pages 86 and 87 above.

Quantified and unquantified risks are listed separately. Within each list the risks have been categorised as new or changed/unchanged since the last Economic and Fiscal Update.

Risks are unquantified if the amount of the risk is unknown, or if the matter is partially disclosed as an unquantified risk (as full disclosure would be likely to prejudice New Zealand’s substantial economic interests, security, defence or international relations; or compromise the Crown in a material way in negotiation, litigation or commercial activity; or result in a material loss of value to the Crown).

Fuller descriptions of the risks listed below are included on pages 94 to 103.

Quantified Risks

If they were to eventuate the risks outlined in these tables would, to the extent that they cannot be funded from future budget allowances, by reprioritising existing expenditure or through third-party revenue, impact the Government’s forecast financial position (as indicated in the table below).

A negative fiscal impact means an increase in net debt and possibly a decrease in the operating balance.

Quantified risks as at 4 May 2010	Impact on fiscal position	Value of risk
New risks		
Economic Development – Venture Investment Fund underwrite	Negative	\$40m
Justice – Auckland Courthouse Capital Programme	Negative	\$160m
Ministerial Services – Rugby World Cup Visits Programme	Negative	\$4m per annum and \$12m one-off
Transport – Support for New Zealand Railways Corporation (KiwiRail) Business Strategy	Negative	\$500m
Changed risks		
Communications – Broadband Investment	Negative	\$1b capital
Corrections – Community Probation and Psychological Services	Negative	\$24m capital and \$30m operating
Corrections – Prison Construction	Negative	\$412m capital and \$63m operating
Education, Social Development, Health and Revenue – Medical Training Places	Negative	\$12m operating per annum
Immigration – Immigration New Zealand Change Programme	Negative	\$63m over 4 years
Justice – Review of the Legal Aid System	Negative	\$274m
Police – Digital Radio Network Phase 2	Negative	\$150m

Quantified risks as at 4 May 2010	Impact on fiscal position	Value of risk
Unchanged risks		
Defence Force – Future Operationally Deployed Forces Activity	Negative	\$30m operating
Defence Force – Sale of Skyhawks and Aermacchi Trainers	Positive	\$130m
Education – Broadband Investment: Schools	Negative	\$150m to \$235m
Finance – Crown Overseas Properties	Negative	Preliminary cost estimates total \$150m over the period 2009/10 to 2013/14
Health – Additional WellChild Visits	Negative	\$15.4m per annum
Immigration – Re-development of Mangere Refugee Centre	Negative	\$5m operating and \$25m capital

Unquantified Risks

If they were to eventuate the risks outlined in these tables would, to the extent that they cannot be funded from future budget allowances, by reprioritising existing expenditure or through third-party revenue, impact the Government's forecast financial position (as indicated in the table below).

A negative fiscal impact means an increase in net debt and possibly a decrease in the operating balance.

Unquantified risks as at 4 May 2010	Impact on fiscal position
New risks	
ACC – Levies and Non-Earners' Account	Positive or Negative
Broadcasting – Digital Switchover	Negative
Climate Change – Finance for Developing Countries	Negative
Finance – Electricity Reforms	Negative
Housing – State Housing Tenancy Management	Negative
Research, Science and Technology – Research Infrastructure	Negative
Revenue – Review Tax Treatment of Fitout of Commercial and Industrial Buildings	Positive or Negative
Revenue – Reviews Stemming from Budget 2010 Tax Changes	Positive or Negative
Transport – Changes to Penalties for Driving Offences	Negative
Changed risks	
Economic Development – Large Budget Screen Production Fund	Negative
Education – Additional Funding for School Property	Negative
Health – Caregiver Employment Conditions	Negative
Health – H1N1 Pandemic	Negative
Health – Payment of Family Caregivers	Negative

Unquantified risks as at 4 May 2010	Impact on fiscal position
Unchanged risks	
Climate Change – ETS and International Climate Change Obligations	Positive or Negative
Defence Force – Defence Review	Negative
Education – School Operational Grants	Negative
Education – Additional Funding for Defective School Buildings	Negative
Education – Early Childhood Education Participation	Negative
Finance – Crown Retail Deposit Guarantee Scheme	Negative
Finance – Government Commitments to International Financial Institutions	Negative
Finance – New Zealand Post Equity Injection to Fund Expansion	Negative
Health – District Health Board Deficits	Negative
Housing – Hobsonville Urban Development	Negative
Housing – Weathertight Homes	Negative
Revenue – Cash Held in Tax Pools	Negative
Revenue – Charitable Giving	Negative
Revenue – Child Support - Shared Care	Negative
Revenue – Imputation	Negative
Revenue – International Tax Review	Negative
Revenue – Redesigning Business Processes at Inland Revenue	Positive
Revenue – Potential Tax Policy Changes	Positive or Negative
Revenue – Tax Issues Relating to Auckland Governance Reform	Positive or Negative
Transport – Tauranga Eastern Corridor	Negative
Risk to Third-Party Revenue	Negative
State Sector Employment Agreements	Negative
Reviews of the Delivery of Public Services	Positive

Risks Removed Since the 2009 Half Year Economic and Fiscal Update

The following risks have been removed since the 2009 Half Year Economic and Fiscal Update:

Expired risks	Reason
ACC – Levy increases	2010/11 levies are now finalised and their effect is included in the forecasts
Customs – Joint Border Management System Replacement	Systems development is being funded in Budget 2010
Defence Force – Project Protector Warranty Issues	Project Protector mediation now complete and full and final warranty payments confirmed
Education – Early Childhood Education Ratio Changes	No longer likely
Education – School Staffing Entitlements	Decision taken in Budget 2010
Education – Demand for Tertiary Education	Decision taken in Budget 2010
Education – Early Childhood Education Funding	Decision taken in Budget 2010
Education – Integrated School property	Decision taken in Budget 2010
Education – Te Whare Wānanga o Awanuiārangi	Decision taken in Budget 2010
Education – Trades Academies	No longer meets \$10m threshold for disclosure
Finance – New Zealand Superannuation Fund	No longer likely
Health – Funding Increase for Subsidised Medicines	No longer likely
Health – National systems development programme	Programme no longer running, no further funding sought
Housing – Tamaki	No longer likely
Justice – Greater Auckland Service Delivery Strategy	Included in Budget 2010 contingencies for Audio Visual Links and Criminal Procedure Simplification
Justice – Family Court Professional Services	Funded as an initiative in the Justice Allocation in Budget 2010
Revenue – Goods and Services Tax - Business to Business Transactions	Revenue increases have been incorporated within baselines
Revenue - KiwiSaver	Has been included in the fiscal forecast assumptions
Revenue - Mutual Recognition and the Australian Tax Review	No longer likely
Revenue – Possible Structural Tax Changes	This risk is superseded by the Budget 2010 tax package
Revenue – Reducing Compliance Costs for Small- and Medium-sized Enterprises	No longer likely
Revenue – Reinstatement of Deferred Tax Cuts	This risk is superseded by the Budget 2010 tax package
Revenue – Revenue Implications of Recommendations from the Capital Market Development Taskforce	Recommendations have been published, risk now incorporated in "Potential Tax Changes" risk

Expired risks	Reason
Revenue – Tax Treatment of Social Assistance Programmes	This risk is superseded by the Budget 2010 tax package
Social Development – Increasing the Abatement-Free Income Threshold	The Government has agreed to increase the abatement-free threshold as part of the Future Focus package of benefit reforms
State Services – KiwiSaver Contribution	Covered by generic risk and included in forecasts
Tourism – Investment in Tourism Infrastructure	No longer likely
Transport – NZRC Operating Support and Loans	Superseded by KiwiRail risk

Statement of Specific Fiscal Risks

ACC – Levies and Non-Earners' Account (new, unquantified risk)

Changes in tax settings and ACC's financial performance affect the Crown's levy income and liability for claims. The lag between half-yearly liability valuation and annual decisions on levies means that future levy rates may differ from current levels, with either a positive or negative impact on revenue.

Broadcasting – Digital Switchover (new, unquantified risk)

The Government is planning to announce a date for digital switchover (DSO) when take-up of digital TV reaches 75% or 2012, whichever is the earlier. Depending on the date chosen for DSO, and the level of any direct support that the Government chooses to provide to assist smooth transition and thereby ensure that maximum potential economic benefit is realised, there may be a negative impact on the operating balance.

Climate Change – ETS and International Climate Change Obligations (unchanged, unquantified risk)

There is uncertainty in the level of fiscal impact associated with the Kyoto obligation over the 2008-2012 first commitment period. The net impact of variables including carbon prices, levels of net emissions, the uptake of post-1989 foresters and allocation levels to emitters are highly uncertain and could change the Government's costs significantly. A review of the Emissions Trading Scheme (ETS) in 2011 may also have fiscal implications. The Government may need to purchase emission units to meet its obligations under the Climate Change Response Act 2002 and the Kyoto protocol, with a corresponding impact on net debt.

After the first commitment period, no rights or obligations are forecast in the Government's accounts for any post-2012 international climate change agreement, given the Government has yet to ratify any such agreement and the high levels of uncertainty around its potential nature and size. Also, the effect of the ETS, which transfers the impact of the world price of carbon through the economy, will mitigate the fiscal impact of such an agreement. Any agreement entered into will need to be recognised at the time, alongside forecast ETS revenues and expenses.

Climate Change – Finance for Developing Countries (new, unquantified risk)

There is an international expectation that developed countries, including New Zealand, contribute finance to developing countries to support adaptation and mitigation. Globally, contributions are likely to be in the order of tens to hundreds of US billions of dollars per year from this year onward. Following the Copenhagen climate change negotiations in 2009, New Zealand associated with the Copenhagen Accord. In the Accord, developing countries committed to contribute finance to developing countries to support mitigation and adaptation, collectively approaching US\$30 billion over 2010-2012 and US\$100 billion per annum by 2020. New Zealand's contribution as a portion of this finance is currently uncertain.

Communications – Broadband Investment (changed, quantified risk)

The Government has committed to spend \$1.5 billion on a new broadband network delivering “ultra fast” broadband services. Of this amount, \$290 million has been appropriated through Budget 2009 and \$258 million through Budget 2010. The timing and amount of further funding has not yet been determined.

Corrections – Community Probation and Psychological Services (changed, quantified risk)

The 2009-2017 Criminal Justice Forecast predicts a significant increase in the number of sentences and orders served in the community over the forecast period. The Department of Corrections estimates that this would require an additional 497 Probation Officers, Programme Facilitators and Psychologists over the forecast period based on current levels of service delivery. This size of this risk has decreased since the last Economic and Fiscal Update because the Department is able to absorb part of the increase within baselines. The Department now estimates that it will require an additional \$30 million operating by 2013/14 and additional capital funding of \$24 million.

Corrections – Prison Construction (changed, quantified risk)

The Government is considering options to address forecast growth in the prison population. Under current policy settings, the Department of Corrections faces prison capacity demands over the next 10 years. The Department has developed a plan to respond to this demand by increasing prison capacity and replacing capacity that is at the end of its life. The first stage of this plan (a new prison at Wiri and expansion of Mt Eden Prison) received funding in Budget 2010. If the Government chooses to fund the remainder of this plan, it would cost up to an additional \$412 million capital over the next 10 years and \$63 million operating per annum by 2018/19. These figures are subject to change depending on the procurement methods chosen by the Government.

Defence Force – Defence Review (unchanged, unquantified risk)

The Government has approved terms of reference for a Defence Review and subsequent Defence White Paper. This process is expected to be completed by 30 September 2010. Included in the Defence Review is an examination of financial management procedures to meet the long-term defence funding requirements. The Defence Review is likely to present a range of options with different funding implications.

Defence Force – Future Operationally Deployed Forces Activity (unchanged, quantified risk)

There are currently over 400 New Zealand Defence Force personnel deployed overseas on peace-keeping and United Nations missions. Maintaining existing deployment levels would result in an increased annual operating balance impact of some \$30 million from 2011/12 subject to any decisions to change existing deployments. The forthcoming White Paper on Defence expected to be completed by 30 September 2010 will consider future funding requirements for a range of operational commitments in the context of Government’s wider policy priorities and fiscal position.

Defence Force – Sale of Skyhawks and Aermacchi Trainers (unchanged, quantified risk)

New Zealand's application to sell the former Air Combat Force aircraft has been approved by the US Congress and now depends on the successful conclusion of commercial negotiations. Should the sale proceed, at a contract value of US\$110 million, the net proceeds from the sale are expected to be around NZ\$130 million.

Economic Development – Large Budget Screen Production Fund (changed, unquantified risk)

The Large Budget Screen Production Fund is a fund to assist film production companies. The appropriation is set at \$36 million, however the Fund is a demand-driven programme and actual costs are dependent upon the number of productions. In any given year, the number of productions underway can vary and associated costs can vary.

Economic Development – Venture Investment Fund Underwrite (new, quantified risk)

The Government has agreed in principle to provide a four-year \$40 million underwrite to the New Zealand Venture Investment Fund (NZVIF) to allow NZVIF to continue to engage with prospective venture capital fund managers. Approval of the underwrite is subject to further advice from officials.

Education – Broadband Investment: Schools (unchanged, quantified risk)

Government has signalled an investment of \$150 million into Vote Communications to support the introduction of ultra-fast broadband into schools. The capital cost of upgrading school internal networks for all state and state-integrated schools has been estimated at \$235 million. Further work is being undertaken to refine this cost in the coming year.

Education – School Operational Grants (unchanged, unquantified risk)

The Government has historically increased school operating grants in each Budget. Any funding for school operations grants would depend on the circumstances and the ability of the proposal to be funded within existing baselines.

Education – Additional Funding for Defective School Buildings (unchanged, unquantified risk)

As in other areas of the building sector, the school property portfolio has a portion of the building stock built between 1995 and 2005, which is subject to the "leaky buildings" (defective building) issues as a result of poor design, inappropriate materials, poor workmanship and deficient building project oversight.

Education – Additional Funding for School Property (changed, unquantified risk)

The Ministry of Education advises an additional \$154 million may be required for new schools over the next three financial years to meet demographic changes. The Ministry also advises that there is a risk of further increases around the annual property portfolio revaluation which will require increased depreciation funding.

Education – Early Childhood Education Participation (unchanged, unquantified risk)

The Government is considering ways in which early childhood education participation of groups that are currently under-represented might be increased. Any costs would depend on the option chosen and the ability of the proposal to be funded within existing baselines. Currently, the Ministry's Performance Improvement Actions expect increased participation amongst under-represented groups. This is to be funded from savings from the Budget 2009 forecast Early Childhood Education expenditure. However, the Ministry has yet to realise the necessary savings. Because the final costs for a package depend on behavioural changes, this risk is unquantifiable at present, and may vary from costs agreed in Budget 2010.

Education, Social Development, Health and Revenue – Medical Training Places (changed, quantified risk)

The Government has considered funding 200 additional medical training places over five years. Sixty additional medical places were funded in Budget 2009, with a further twenty in Budget 2010. Proceeding with the remaining 120 places would require additional funding, although final costs would depend on the option chosen and the ability of the proposal to be funded within existing baselines. The estimated impact would be \$12 million operating per annum by the end of 2014/15, and this grows beyond the forecast period.

Finance – Crown Overseas Properties (unchanged, quantified risk)

The Government holds New Zealand House in London on a long-term lease from the Crown Estate (UK). Depending on the Government's future intentions for this building, an upgrade may be required. Preliminary cost estimates for this upgrade total \$150 million over the period 2010/11 to 2013/14.

Finance – Crown Retail Deposit Guarantee Scheme (unchanged, unquantified risk)

The Government operates an opt-in Retail Deposit Guarantee Scheme over financial institution deposits. The objective of the scheme is to ensure ongoing retail depositor confidence in New Zealand's financial system, given the international financial market turbulence. A total of 73 financial institutions have been approved under the scheme. These are listed on the Treasury website. Deposits totalling \$133 billion are under guarantee. The Crown also continually updates the likelihood of further default actions triggering the guarantee and assesses the expected loss given default. Based on these assessments, the Crown has provided for \$881 million as at 31 March for future payments under this scheme after expected recoveries. The policy decision to extend and amend the Retail Deposit Guarantee Scheme to 31 December 2011 was announced on Tuesday 25 August 2009 and as at 30 April 2009, 4 financial institutions had been approved under the extended guarantee. This reflects the significant uncertainty as to the value that can be realised from an entity's assets following an event of default. Except as provided on the Treasury website, further information on the Retail Deposit Guarantee Scheme cannot be provided due to commercial sensitivity.

Finance – Electricity Reforms (new, unquantified risk)

In December 2009, the Government announced a series of measures related to improving the operation of the electricity market, including reconfiguring State-Owned Enterprises' assets (virtual and physical asset swaps), a liquid hedge market, and measures to improve security of supply. Some details of these measures are yet to be decided; for example, the timing for the SOE asset reconfiguration. Given this, the impact of the reforms on the individual SOEs cannot currently be estimated. While some aspects of the measures, such as the physical asset swaps between Meridian and Genesis, should be fiscally neutral for the Crown as owner of the SOEs, other aspects may not be, but this cannot currently be quantified. There are also implementation costs associated with the reforms, estimated to be between \$6 million and \$12 million.

Finance – Government Commitments to International Financial Institutions (unchanged, unquantified risk)

The forecast level of government commitments to international financial institutions is subject to change, depending on the Government's response to any changed financial plans on the part of these institutions.

Finance – New Zealand Post Equity Injection to Fund Expansion (unchanged, unquantified risk)

A decision to fund New Zealand Post's business expansion through equity injection or other form of financial support is currently being sought.

Health – Additional WellChild Visits (unchanged, quantified risk)

The Government is considering providing funding for three additional WellChild visits during the first nine weeks of a baby's life. The initiative has not been funded in Budget 2009 or Budget 2010, and has been deferred for consideration in future Budgets. If approved, the indicative cost of this initiative would be \$15 million operating in 2011/12 and outyears.

Health – Caregiver Employment Conditions (changed, unquantified risk)

The Employment Court has made a judgement in favour of two third-party employed caregivers regarding their sleepover employment conditions. Although the third-party employer is appealing the decision, an unsuccessful result would require consideration of the repercussions for the Crown.

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

Several District Health Boards (DHBs) have projected operating deficits in 2010/11. The Government has stated that it does not view projected DHB operating deficits as acceptable, and the Ministry of Health is working with DHBs to develop financial recovery plans. The Government has set aside funding in Vote Health to meet deficit requirements in 2010/11, anticipating that the DHB deficit position will improve in future years.

Health – H1N1 Pandemic (changed, unquantified risk)

In the event of a second wave H1N1 pandemic, there may be fiscal impacts as a result of an increase in demand for Tamiflu and antibiotics, and an increase in the utilisation of medical facilities.

Health – Payment of Family Caregivers (changed, unquantified risk)

The Human Rights Tribunal has declared that the Ministry of Health’s policy of not employing family members to provide care to disabled relatives is in breach of S19 of the New Zealand Bill of Rights. An appeal has been lodged in the High Court.

Housing – Hobsonville Urban Development (unchanged, unquantified risk)

The Government has commenced the development of an integrated urban community at Hobsonville within an area known as the Buckley precinct. Funding was provided in Budget 2008 for this precinct, as well as any other costs that will be incurred concurrently in order to enable broader site works and whole of project infrastructure. Additional capital funding may be required for the subsequent precincts in future Budgets. This would increase net debt until 2013 when the development will begin providing a return to the Crown. This risk is unquantified as disclosure could compromise the Government in negotiations with potential private sector partners.

Housing – State Housing Tenancy Management (new, unquantified risk)

The Government is considering changing tenancy management practices for state house tenants, with the aim of increasing the proportion of houses that are occupied by high needs tenants. This is likely to result in higher costs to the Crown for the Income Related Rent subsidy paid to the Housing New Zealand Corporation and the Accommodation Supplement. The changes could also increase public expectations that all high needs applicants are housed, which could lead to pressure to increase the size of the state housing portfolio.

Housing – Weathertight Homes (unchanged, unquantified risk)

The Government is considering options to facilitate assistance to homeowners to repair homes affected by the weathertightness issues that occurred as a result of changes to building regulations and industry practices in the late 1990s and early 2000s.

Immigration – Immigration New Zealand Change Programme (changed, quantified risk)

The Immigration New Zealand Change Programme proposes an integrated approach to upgrading immigration services. Work is underway and further work is proposed, particularly a significant upgrade of existing ICT systems. Were the ICT component to proceed, estimated Crown capital costs are up to \$62 million over four years from 2010/11 to 2013/14. Ongoing costs of the project would be funded from fees.

Immigration – Re-development of Mangere Refugee Centre (unchanged, quantified risk)

The existing refugee facilities at Mangere may need refurbishment. Initial estimated costs of the refurbishment are \$5 million operating and \$25 million capital.

Justice – Auckland Courthouse Capital Programme (new, quantified risk)

Forecast level of demand for court services under current policy settings indicates there may be a need for additional courthouse capacity in the greater Auckland region. If additional funding is provided, the overall estimated cost will be up to \$160 million with \$20 million in 2011/12, \$25 million in 2012/13 and \$115 million in 2013/14. The Minister of Finance has yet to fully consider the quantum of this risk.

Justice – Review of the Legal Aid System (changed, quantified risk)

The Government has already taken a number of steps to improve the administration of the legal aid system. The Government is developing further options for delivering legal aid services in a sustainable and affordable way. Final costs will depend on the further decisions that are expected to be taken in early 2011.

Ministerial Services – Rugby World Cup Visits Programme (new, quantified risk)

It is expected that the costs of the guest of government and state functions programme will be higher than usual during the year of the Rugby World Cup. It is currently estimated that, beyond the annual budget of \$4 million, a further \$12 million will be spent on showcasing New Zealand to a wide range of overseas visitors coming to New Zealand in connection with the event. These costs include official events, accommodation and hospitality for the guests of government.

Police – Digital Radio Network Phase 2 (changed, quantified risk)

The Government has previously funded the partial implementation of a Digital Radio Network in Wellington, Auckland and Christchurch, to be completed by December 2010. Police are still considering options for the further rollout of a National Digital Radio Network, possibly beginning in the 2011/12 fiscal year. Earlier estimates suggested costs of up to \$150 million, comprising \$28 million in capital in 2011/12, rising to \$38 million in 2013/14; and \$7 million of operating in 2011/12, rising to \$18 million in 2013/14.

Research, Science and Technology – Research Infrastructure (new, unquantified risk)

The Government is considering a five year Research Infrastructure Strategy for Vote Research, Science and Technology. Current planning indicates this will cost \$130 million to \$200 million over five years. Any costs that are not able to be funded within baselines will decrease the operating allowance.

Revenue – Cash Held in Tax Pools (unchanged, unquantified risk)

Funds held in tax pools are recognised as an asset to the Crown. There is a risk that funds held in these pools, over and above a customer’s provisional tax liability, may be withdrawn, resulting in an unquantified cash loss to the Crown.

Revenue – Charitable Giving (unchanged, unquantified risk)

Officials are investigating possible tax incentives for charitable giving, including gift aid and changes in the tax treatment of cultural gifts.

Revenue – Child Support – Shared Care (unchanged, unquantified risk)

A Government discussion document will be released on shared care in the child support formula, including taking into account the incomes of both parents and the costs of children. Any changes would have administrative costs for Inland Revenue and could have further costs to Government from reduced offsets to benefits.

Revenue – Imputation (unchanged, unquantified risk)

Aspects of the current imputation system are being reviewed. This includes whether companies should be able to stream imputation credits, and the refundability of imputation credits, particularly to charities.

Revenue – International Tax Review (unchanged, unquantified risk)

A number of proposals will be considered, and possibly progressed, as part of Phase II of the international tax review. Since all these proposals involve exempting income in particular circumstances, they may, if progressed, have a negative impact on tax revenue.

Revenue – Redesigning Business Processes at Inland Revenue (unchanged, unquantified risk)

The Government is investigating options to redesign business processes at Inland Revenue, which could include both policy and administrative options to simplify customer interactions in the Pay As You Earn and Personal Tax Summary systems. Any changes could impact tax revenue collections or have material administrative costs to implement.

Revenue – Potential Tax Policy Changes (unchanged, unquantified risk)

The Government is considering changes to various tax policies as indicated in the 18 month tax policy work programme. Measures on the current work programme are expected to be revenue neutral in aggregate. Measures enacted to date, and included in revenue forecasts, have increased tax revenue by around \$50 million per annum. The remaining items are expected to be revenue negative up to the same extent. Because it is unclear exactly what additional policy changes, if any, will be made at this stage, these further changes have not been included in revenue forecasts. The work programme will be revised as soon as possible after the Budget.

Revenue – Review Tax Treatment of Fitout of Commercial and Industrial Buildings (new, unquantified risk)

The Government has announced a review of the appropriate tax treatment for “fitouts” of commercial and industrial buildings in light of Inland Revenue’s interpretation statement IS10/01 on the treatment of residential building fitout. Depending on the outcome of that review, there could be a fiscal gain or loss over the forecast period.

Revenue – Reviews Stemming from Budget 2010 Tax Changes (new, unquantified risk)

The tax changes announced in Budget 2010 include commencing consultation on the exact nature of policy changes that will be legislated later in 2010 for enactment from 1 April 2011. To the extent that consultation leads to enacted legislation that is different from what is currently expected, the revenue implications of policy changes may be different from what is forecast.

Revenue – Tax Issues Relating to Auckland Governance Reform (unchanged, unquantified risk)

New entities are likely to emerge from the reform of local governance in Auckland. Some of these new entities could have tax liabilities different to the tax liabilities of existing entities, which would impact on the total tax paid by Auckland local government entities beyond the 1 November 2010 transition date. Depending on the shape of entities adopted, the changes could decrease tax revenue.

Reviews of the Delivery of Public Services (unchanged, unquantified risk)

The Government has announced its intention to deliver more public services, more effectively, for fewer resources. The Government may undertake one or a number of value-for-money in-depth reviews over the next 12 months. The Government has also agreed to the implementation of a number of Performance Improvement Actions (PIAs). Reviews and PIAs may identify areas of expenditure that are not efficient, effective or aligned to government policy, or could be delivered differently. Reviews and PIAs may recommend, or result in, changes to service delivery and/or free up resources for reprioritisation within the vote (or within the organisation) or be returned to the centre to meet pressures in other areas. Reviews of government activities that result in improved cost-effectiveness are likely to have a positive impact on the fiscal position.

Risk to Third-Party Revenue (unchanged, unquantified risk)

A wide range of government activities are funded through third-party fees and charges. With a decrease in economic activity, there is a risk that decreases in third-party revenue streams will require changes to service delivery with transitional costs to the Crown. For example, decreases in Customs revenue or in levies on building activity may mean that some activities are temporarily unable to be fully cost-recovered and the Government will need to transition out of an activity or temporarily subsidise that activity.

State Sector Employment Agreements (unchanged, unquantified risk)

A number of large collective agreements are due to be renegotiated in the short to medium term. As well as direct fiscal implications from any changes to remuneration, the renegotiation of these agreements can have flow-on effects to remuneration in other sectors. The Government has signalled an expectation for restraint given the current economic environment and conditions in the private sector.

Transport – Changes to Penalties for Driving Offences (new, unquantified risk)

The Government is considering changes to driving offences, in particular increasing penalties for driving offences causing injury or death. Final costs will depend on options chosen and may increase costs in Votes Courts, Justice, Attorney-General, Police, and Corrections.

Transport – Support for New Zealand Railways Corporation (KiwiRail) Business Strategy (new, quantified risk)

The Government has agreed in principle to support a 10-year strategy for the New Zealand Railways Corporation (NZRC, trading as KiwiRail Group) to achieve a commercially viable rail network. A total of \$750 million in capital over the next three years is forecasted as the Crown contribution towards the strategy, but its disbursement will be dependent on the approval of suitable business cases and demonstrable progress towards objectives. Budget 2010 has provided \$250 million in capital as the first tranche of Crown funding for this strategy. If this funding results in progress towards the desired service improvements and revenue uplift, and if subsequent business cases can justify further investment, up to \$500 million in additional capital may be required over the next two Budgets. Budget 2010 also provides for the refinancing of \$170 million of NZRC debt to the Crown. In addition to this, NZRC has \$220 million in debt to the Crown maturing over the period 2011/12 to 2014/15, which the Crown may also need to refinance.

Transport – Tauranga Eastern Corridor (unchanged, unquantified risk)

The Crown may be asked to provide a loan to the New Zealand Transport Agency to advance the construction of the Tauranga Eastern Corridor Roading Project. It is intended that the loan will be repaid by toll revenue from the road.

Contingent Liabilities and Contingent Assets

Contingent liabilities are costs that the Crown will have to face if a particular event occurs. Typically, contingent liabilities consist of guarantees and indemnities, legal disputes and claims, and uncalled capital. The contingent liabilities facing the Crown are a mixture of operating and balance sheet risks, and they can vary greatly in magnitude and likelihood of realisation.

In general, if a contingent liability were realised it would reduce the operating balance and increase net debt. However, in the case of contingencies for uncalled capital, the negative impact would be restricted to net debt.

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

Contingent assets are potential assets dependent on a particular event occurring.

Only contingent liabilities and contingent assets involving amounts of over \$10 million are separately disclosed. Contingent liabilities and assets below \$10 million are included in either the “other quantifiable contingent liabilities” total or the “other quantifiable contingent assets” total.

Contingent liabilities and contingent assets have been stated as at 31 March 2010, being the latest set of contingencies reported.

Quantifiable Contingent Liabilities and Contingent Assets

Guarantees and indemnities	Status¹⁰	(\$ million)
Air New Zealand – letters of credit and performance bonds	Changed	61
Cook Islands – Asian Development Bank loans	Changed	14
Indemnification of receivers and managers – Terralink Limited	Unchanged	10
Ministry of Transport – funding guarantee	Unchanged	10
Guarantees and indemnities of SOEs and Crown entities	Changed	8
Other guarantees and indemnities	Changed	13
		116
Uncalled capital		
Asian Development Bank	Changed	1,080
Bank for International Settlements	Changed	26
European Bank for Reconstruction and Development	Changed	14
International Bank for Reconstruction and Development	Changed	1,156
Other	Changed	7
		2,283
Legal proceedings and disputes		
Health legal claims	Unchanged	15
Inland Revenue legal proceedings and disputes – tax	Changed	267
Kapiti West link road	Changed	14
Other legal claims	Changed	46
		342
Other quantifiable contingent liabilities		
Air New Zealand partnership	Changed	61
Crown Health Financing Agency	Changed	26
Inland Revenue – unclaimed monies	Changed	50
International finance organisations	Changed	1,532
Kyoto Protocol units	Changed	1,747
New Zealand Export Credit Office – export guarantees	Changed	145
Reserve Bank – demonetised currency	Unchanged	23
Other quantifiable contingent liabilities of SOEs and Crown entities	Changed	37
Other quantifiable contingent liabilities	Changed	31
		3,652
Total quantifiable contingent liabilities		6,393
Quantifiable contingent assets		
Inland Revenue – legal proceedings and disputes	Changed	199
Ministry of Education – suspensory loans	Changed	66
Other quantifiable contingent assets	Changed	9
Total quantifiable contingent assets		274

¹⁰ Relative to reporting in the 15 December 2009 *Budget Policy Statement 2010*.

Unquantifiable Contingent Liabilities

Guarantees and indemnities	Status¹¹
Airways Corporation of New Zealand Limited	Unchanged
AsureQuality Limited	Unchanged
At Work Insurance Limited	Unchanged
Bona Vacantia property	Unchanged
Building Industry Authority	Unchanged
Contact Energy Limited	Unchanged
Crown Retail Deposit Guarantee Scheme	Unchanged
Earthquake Commission (EQC)	Unchanged
Electricity Corporation of New Zealand Limited (ECNZ)	Unchanged
Ministry of Fisheries – indemnity provided for delivery of registry services	Unchanged
Genesis Power Limited – supply of gas	Unchanged
Genesis Power Limited – contractor claims	New
Genesis Power Limited – financial guarantees	Unchanged
Genesis Power Limited – letters of credit and performance bonds	Unchanged
Housing New Zealand Corporation (HNZC)	Unchanged
Indemnities against acts of war and terrorism	Unchanged
Justices of the Peace, Community Magistrates and Disputes Tribunal Referees	Unchanged
Landcorp Farming Limited	Unchanged
Maui Partners	Unchanged
National Provident Fund	Unchanged
New Zealand Railways Corporation (NZRC)	Unchanged
Persons exercising investigating powers	Unchanged
Public Trust	Unchanged
Reserve Bank of New Zealand	Unchanged
Synfuels-Waitara outfall indemnity	Unchanged
Tainui Corporation	Unchanged
Other unquantifiable contingent liabilities	
Abuse claims	Unchanged
Accident Compensation Corporation (ACC) litigations	Changed
Air New Zealand litigation	Changed
Environmental liabilities	Unchanged
Kordia Group Limited	Unchanged
Maui contracts	Unchanged
Rugby New Zealand 2011 Limited – joint venture arrangements	Unchanged
Television New Zealand Limited	Unchanged
Treaty of Waitangi claims	Unchanged
Treaty of Waitangi claims – settlement relativity payments	Unchanged
Westpac Banking Corporation	Unchanged
Other contingencies	
Foreshore and seabed	Unchanged

¹¹ The following unquantified contingent liability was removed: Geothermal carbon tax indemnity.

Statement of Contingent Liabilities and Contingent Assets

Quantifiable contingent liabilities

Guarantees and indemnities

Guarantees and indemnities are disclosed in accordance with NZ IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. In addition, guarantees given under section 65ZD of the Public Finance Act 1989 are disclosed in accordance with section 26Q(3)(b)(i)(B) of the same Act.

Air New Zealand – letters of credit and performance bonds

The letters of credit are primarily given in relation to passenger charges, airport landing charges and indemnities provided to financial institutions on limits provided on staff credit cards. The performance bonds are primarily given in respect to engineering contracts.

\$61 million at 31 March 2010 (\$32 million at 31 October 2009)

Cook Islands – Asian Development Bank (ADB) loans

Before 1992, the New Zealand Government guaranteed the Cook Islands' borrowing from the ADB. These guarantees have first call on New Zealand's Official Development Assistance.

\$14 million at 31 March 2010 (\$15 million at 31 October 2009)

Indemnification of receivers and managers – Terralink Limited

The Crown has issued a Deed of Receivership indemnity to the appointed receivers of Terralink Limited against claims arising from the conduct of the receivership.

\$10 million at 31 March 2010 (\$10 million at 31 October 2009)

Ministry of Transport – funding guarantee

The Minister of Finance has issued a guarantee of \$10 million to the Transport Accident Investigation Commission. The guarantee allows the Commission to assure payment to suppliers of specialist salvage equipment in the event of the Commission initiating an urgent investigation of any future significant transport accident.

\$10 million at 31 March 2010 (\$10 million at 31 October 2009)

Legal proceedings and disputes

The amounts under quantifiable contingent liabilities for legal proceedings and disputes are shown exclusive of any interest and costs that may be claimed if these cases were decided against the Crown.

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

Health legal claims

Claims against the Crown in respect of alleged negligence for failing to screen blood for Hepatitis C when screening had first become available, resulting in people allegedly contracting Hepatitis C through contaminated blood and blood products.

\$15 million at 31 March 2010 (\$15 million at 31 October 2009)

Inland Revenue legal proceedings and disputes – tax

Legal proceedings and disputes tax represents the outstanding debt of those tax assessments raised, against which an objection has been lodged and legal action is proceeding. When a taxpayer disagrees with an assessment issued following the dispute process, the taxpayer may challenge that decision by filing proceedings with the Taxation Review Authority or the High Court.

The reduction in contingent liabilities is owing to the dispute with a number of financial institutions regarding the tax treatment of certain structured finance transactions, which has now been settled.

\$267 million at 31 March 2010 (\$1,655 million at 31 October 2009)

Kapiti West link road

Court action has been filed against New Zealand Transport Agency to have the land held for the Kapiti West link road released for sale. The maximum liability is \$14 million.

\$14 million at 31 March 2010 (\$25 million at 31 October 2009)

Other quantifiable contingent liabilities

Air New Zealand partnership

The Air New Zealand Group has a partnership agreement with Christchurch Engineering Centre in which it holds 49 % interest. By the nature of the agreement joint and several liability exists between the two parties.

\$61 million at 31 March 2010 (\$68 million at 31 October 2009)

Crown Health Financing Agency

The agency is subject to potential legal claims plus associated legal fees in respect of the actions of the former Area Health Boards. The agency is defending those claims that have resulted in litigation and will defend any of the others that result in litigation. The agency does not accept liability for the claims.

\$26 million at 31 March 2010 (\$28 million at 31 October 2009)

Inland Revenue – unclaimed monies

Under the Unclaimed Monies Act 1971, companies (eg, financial institutions, insurance companies) hand over money not claimed after six years to Inland Revenue. The funds are repaid to the entitled owner on proof of identification.

\$50 million at 31 March 2010 (\$46 million at 31 October 2009)

International finance organisations¹²

The Crown has lodged promissory notes with the International Monetary Fund. Payment of the notes depends upon the operation of the rules of the organisation.

\$1,532 million at 31 March 2010 (\$1,561 million at 31 October 2009)

Kyoto Protocol units

During the first commitment period the Net Kyoto Position of the Crown estimates that 89.1 million tonnes of carbon credits will be generated by carbon removals via forests. To the extent that these forests are harvested in subsequent commitment periods there will be an associated liability generated that will need to be repaid.

The New Zealand Emissions Trading Scheme transfers a portion of the potential future liability to forest owners. As at 31 March 2010, approximately three million tonnes has been transferred to forest owners in the form of New Zealand units. The Crown's contingent liability is calculated as the remaining credits the Crown is potentially liable for (86.1 million tonnes) multiplied by the carbon price of \$20.29 as at 31 March 2010.

\$1,747 million at 31 March 2010 (\$1,871 million at 31 October 2009)

New Zealand Export Credit Office – export guarantees

The New Zealand Export Credit Office (NZECO) provides a range of guarantee products to assist New Zealand exporters. These NZECO guarantees are recorded by the Crown as contingent liabilities. The amount of future liabilities arising from these guarantees is expected to be minor.

\$145 million at 31 March 2010 (\$175 million at 31 October 2009)

Reserve Bank – demonetised currency

The Crown has a contingent liability for the face value of the demonetised currency issued which has yet to be repatriated.

\$23 million at 31 March 2010 (\$23 million at 31 October 2009)

Unquantifiable contingent liabilities

Accounting standard NZ IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* requires that contingent liabilities be disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. Disclosure of remote contingent liabilities is only required if knowledge of the transaction or event is necessary to achieve the objectives of general purpose financial reporting. This part of the statement provides details of those contingent liabilities of the Crown that cannot be quantified (remote contingent liabilities are excluded).

¹² On 13 April 2010 the Minister of Finance announced that New Zealand had agreed to make available to the International Monetary Fund up to US\$1 billion (NZ\$1.3 billion approximately) to support the international financial system in the event of a significant crisis.

*Guarantees and indemnities***Airways Corporation of New Zealand Limited**

The Crown has indemnified Airways Corporation of New Zealand Limited as contained in Airways' contract with New Zealand Defence Force for the provision of air traffic control services. The indemnity relates to any claim brought against Airways by third parties arising from military flight operations undertaken by the Royal New Zealand Air Force.

AsureQuality Limited

The Crown has indemnified the directors of AsureQuality Limited in the event that they incur any personal liability for redundancies arising from any agreement by international trading partners that allows post-mortem meat inspection by parties other than the Ministry of Agriculture and Forestry, or its sub contractor.

At Work Insurance Limited

The Crown has indemnified the liquidators of At Work Insurance Limited (Deloitte Touche Tohmatsu) against various employment-related claims.

Bona Vacantia property

P&O NZ Limited sought a declaratory judgement that property disclaimed by a liquidator is bona vacantia. A settlement has been reached, which includes a Crown indemnity in favour of New Zealand Aluminium Smelters and Comalco in relation to aluminium dross disposed of in their landfill, for costs that may be incurred in removing the dross and disposing of it at another site if they are required to do so by an appropriate authority. The Minister of Finance signed the indemnity on 24 November 2003. In February 2004, a similar indemnity was signed in respect of aluminium dross currently stored at another site in Invercargill.

Building Industry Authority

The Building Industry Authority (BIA) is a joint defendant in a number of claims before the courts and the Weathertight Homes Resolution Service relating to the BIA's previous role as regulator of the building industry. The BIA has been disestablished and absorbed into the Department of Building and Housing and, to prevent conflicts of interest, the Treasury was given responsibility for managing weathertight claims against the BIA on behalf of the Crown from 1 July 2005.

Contact Energy Limited

The Crown and Contact Energy signed a number of documents to settle in full Contact Energy's outstanding land rights and geothermal asset rights at Wairakei. Those documents contained two reciprocal indemnities between the Crown and Contact Energy to address the risk of certain losses to the respective parties' assets arising from the negligence or fault of the other party.

Crown Retail Deposit Guarantee Scheme

On 12 October 2008, the Minister of Finance initiated an opt-in Retail Deposit Guarantee Scheme. The objective of this scheme is to ensure ongoing retail depositor confidence in New Zealand's financial system given the international financial market turbulence.

As at 31 March 2010, 73 financial institutions had joined the scheme and deposits totalling \$132.5 billion had been guaranteed. This is the maximum exposure and does not include any offset resulting from the recovery of the remaining assets of the financial institution in the event the guarantee is called upon. The Crown assesses the potential loss to be associated with the entities that hold significant deposits (ie, greater than \$5 billion) as being remote.

For other entities within the scheme (ie, entities that hold deposits less than \$5 billion) a provision has been made to provide for losses that are considered more likely than not to occur. The Crown continually updates both the likelihood of further default actions triggering the guarantee and the expected loss given default. Based on these assessments, the Crown has provided for a net expected loss given default of \$881 million as at 31 March 2010 (\$899 million at 31 October 2009) being the cost of future payments under the scheme after expected recoveries.

While the provision represents a best estimate of likely loss, a significant range of outcomes is possible under the scheme in terms of which entities may default and the eventual loss to the Crown following an event of default. This reflects the significant uncertainty as to the value that can be realised from an entity's assets following an event of default. Except as provided on the Treasury website, further information on the Retail Deposit Guarantee Scheme cannot be provided owing to commercial sensitivity.

Earthquake Commission (EQC)

The Crown is liable to meet any deficiency in the EQC's assets in meeting the Commission's financial liabilities (section 16 of the Earthquake Commission Act 1993). In the event of a major natural disaster the Crown may be called upon to meet any financial shortfall incurred by the Commission.

Electricity Corporation of New Zealand Limited (ECNZ)

The Deed of Assumption and Release between ECNZ, Contact Energy Limited and the Crown provides that Contact Energy stands in the place of ECNZ for those assets transferred to Contact Energy from ECNZ. As a result of the split of ECNZ, Ministers have transferred the benefits of the Deed to ECNZ's successors – Meridian Energy Limited, Mighty River Power Limited, and Genesis Power Limited.

The liability is open-ended and is of significant commercial value. Directors are unlikely to forego the indemnity without substantial compensation.

As a result of the 1999 split of ECNZ into three new companies the Crown has signed a Deed of Indemnity that has indemnified ECNZ in relation to all ECNZ's pre-split liabilities and any liabilities that arise out of the split itself. This indemnity is provided to ECNZ to ensure that directors can be satisfied as to the ongoing solvency of ECNZ following the split and to enable most of ECNZ's surplus funds to be distributed to the Crown. In addition, the Crown has indemnified ECNZ against any liability that might arise under its debt and swap arrangements as a result of ECNZ entering into the Agreements for Sale and Purchase on 22 December 1998.

In addition, the Crown has guaranteed ECNZ's existing hedge contract obligations, which remain with ECNZ after the split. The principal purpose of the guarantee is to provide sufficient credit support to ECNZ under the hedge contracts so as to avoid providing hedge counterparties reasonable grounds upon which to terminate their hedge contracts

as a result of the split. In light of the expected future medium-term spot price of electricity, it is expected that most payment flows under the hedge contracts will be from the hedge counterparties to ECNZ, which will then be passed to the new SOEs. All hedges have now expired, although some are in litigation regarding errors in how payments were made.

Ministry of Fisheries – indemnity provided for delivery of registry services

The Crown has indemnified Commercial Fisheries Services Limited against claims made by third parties arising from Commercial Fisheries Services undertaking registry services under contract to the Chief Executive of the Ministry of Fisheries. This indemnity provided under the Fisheries Act 1983 and 1996, expires on 30 September 2010.

Genesis Power Limited – supply of gas

The Crown has entered into a deed with Genesis Energy to share a specified and limited amount of risk around the sufficiency of Genesis Energy's long-term supply of gas to cover the Huntly e3p's (a 385 MW combined cycle gas turbine power station) minimum needs. The agreement sees the Crown compensate Genesis Energy in the event it has less gas than it needs.

Genesis Power Limited – contractor claims

A subcontractor to the Kupe Alliance has presented several claims relating to the construction of the Kupe project. These claims have been disputed by the Kupe operator. There can be no assurances that such claims will not have an adverse impact on Genesis Energy's business, financial condition or results of operations.

Genesis Power Limited – financial guarantees

The company issued financial guarantees to the alliance contractor and other agents of the Kupe joint venture for the full and faithful performance of its subsidiaries in their capacities as joint venture partners, to the extent of their several liabilities under the development agreement.

The company issued a financial guarantee to Energy Clearing House Limited for the full and faithful performance of its subsidiary Energy Online Limited, to the extent of its liabilities for its retail electricity purchases.

These guarantees may give rise to liabilities in the company if the subsidiaries do not meet their obligations under the terms of the respective arrangements.

Genesis Power Limited – letters of credit and performance bonds

The company, as a participant in the electricity market, issued letters of credit to the Energy Clearing House Limited under the markets' security requirements. These letters of credit are issued as part of normal trading conditions and are to ensure there is no significant credit risk exposure to any one market participant.

The company has also issued letters of credit and performance bonds to certain suppliers and service providers under normal trading conditions. The liabilities covered by these arrangements are already provided for in the statement of financial position, and therefore not expected to create any adverse effects on the financial results presented. These are not material to the financial statements.

Housing New Zealand Corporation (HNZC)

HNZC is liable to the owners (ANZ National Bank Limited, Ichthus Limited and Westpac Banking Corporation) of mortgages sold by HNZC during 1992 to 1999 for credit losses they may incur from specified limited aspects of their ownership of those mortgages with the Crown standing behind this obligation.

The Crown has provided a warranty in respect of title to the assets transferred to Housing New Zealand Limited (HNZL) (HNZL was incorporated into the HNZC Group as a subsidiary in 2001 as part of a legislated consolidation of government housing functions) and has indemnified HNZL against any breach of this warranty. In addition, the Crown has indemnified HNZL against any third-party claims that are a result of acts or omissions prior to 1 November 1992. It has also indemnified the directors and officers of HNZL against any liability consequent upon the assets not complying with statutory requirements, provided it is taking steps to rectify any non-compliance.

Indemnities against acts of war and terrorism

The Crown has indemnified Air New Zealand against claims arising from acts of war and terrorism that cannot be met from insurance, up to a limit of US\$1 billion in respect of any one claim.

Justices of the Peace, Community Magistrates and Disputes Tribunal Referees

Section 197 of the Summary Proceedings Act 1957 requires the Crown to indemnify Justices of the Peace and Community Magistrates against damages or costs awarded against them as a result of them exceeding their jurisdiction, provided a High Court Judge certifies that they have exceeded their jurisdiction in good faith and ought to be indemnified.

Section 58 of the Disputes Tribunal Act 1988 confers a similar indemnity on Disputes Tribunal Referees.

Landcorp Farming Limited

The Protected Land Agreement provides that the Crown will pay Landcorp any accumulated capital costs and accumulated losses or Landcorp will pay the Crown any accumulated profit, attributed to a Protected Land property that is required to be transferred to the Crown or that the Crown releases for sale. The Crown will also be liable to pay Landcorp, at the time of sale or transfer of any property deemed to be Protected Land, the amount of any outstanding equity payments on the initial value of the property.

Maui Partners

The Crown has entered into confidentiality agreements with the Maui Partners in relation to the provision of gas reserves information. The deed contains an indemnity against any losses arising from a breach of the deed.

National Provident Fund

The National Provident Fund (NPF) has been indemnified for certain potential tax liabilities. Under the NPF Restructuring Act 1990, the Crown guarantees:

- the benefits payable by all NPF schemes (section 60)

- investments and interest thereon deposited with the NPF Board prior to 1 April 1991 (section 61), and
- payment to certain NPF defined contribution schemes where application of the 4% minimum earnings rate causes any deficiency or increased deficiencies in reserves to arise (section 72).

A provision has been made in these financial statements in respect of the actuarially assessed deficit in the DBP Annuitants' Scheme.

[New Zealand Railways Corporation \(NZRC\)](#)

The Crown has indemnified the directors of NZRC against any liability arising from the surrender of the licence and lease of the Auckland rail corridor.

The Crown has further indemnified the directors of NZRC against all liabilities in connection with the corporation taking ownership and/or responsibility for the national rail network and any associated assets and liabilities on 1 September 2004.

On 5 July 2009 the Crown further indemnified the directors of NZRC, and the directors of its subsidiaries, to the same extent that statutory entities can indemnify their members under the Crown Entities Act 2004. This indemnity was given on the grounds that there is no express power in the New Zealand Railways Corporation Act 1981 for New Zealand Railways Corporation to grant its own indemnities.

Section 10 of the Finance Act 1990 guarantees all loan and swap obligations of the NZRC.

[Persons exercising investigating powers](#)

Section 63 of the Corporations (Investigation and Management) Act 1989 indemnifies the Securities Commission, the Registrar and Deputy Registrar of Companies, members of advising committees within the Act, every statutory manager of a corporation and persons appointed pursuant to sections 17 to 19 of the Act, in the exercise of investigating powers, unless the power has been exercised in bad faith.

[Public Trust](#)

Section 52 of the Public Trust Act 2001 provides for the Crown to meet any deficiency in the Public Trust's Common Fund in meeting lawful claims on the Fund. This is a permanent (legislated) liability. On 7 November 2008 the Minister of Finance guaranteed interest payable on estates whose money constitutes the Common Fund.

[Reserve Bank of New Zealand](#)

Section 21(2) of the Reserve Bank of New Zealand Act 1989 requires the Crown to pay the Reserve Bank the amount of any exchange losses incurred by the bank as a result of dealing in foreign exchange under sections 17 and 18 of the Act. This is a permanent (legislated) liability.

[Synfuels-Waitara outfall indemnity](#)

As part of the 1990 sale of the Synfuels plant and operations to New Zealand Liquid Fuels Investment Limited (NZLFI), the Crown transferred to NZLFI the benefit and obligation of a Deed of Indemnity between the Crown and Borthwick-CWS Limited (and subsequent

owners) in respect of the Waitara effluent transfer line that was laid across the Waitara meat processing plant site.

The Crown has the benefit of a counter indemnity from NZLFI that has since been transferred to Methanex Motunui Limited.

Tainui Corporation

Several leases of Tainui land at Huntly and Meremere have been transferred from ECNZ to Genesis Power Limited. The Crown has provided guarantees to Tainui Corporation relating to Genesis Power's obligations under the lease agreements.

Other unquantifiable contingent liabilities

Abuse claims

There is ongoing legal action against the Crown in relation to historical abuse claims. At this stage the number of claimants and outcome of these cases are uncertain.

Accident Compensation Corporation (ACC) litigations

There are legal actions against ACC in existence, arising in the main from challenges to operational decisions made by ACC. In addition, there is an appeal litigation in progress as a consequence of ACC clients appealing a review officer's decision to the District Court. While an estimate of the financial effect of existing legal actions and outstanding appeals cannot be made, ACC believes the resolution of these will not have a materially adverse effect on the financial statements.

Air New Zealand litigation

Air New Zealand has been named in five class actions. One, in Australia, claims travel agents' commission on fuel surcharges and two (one in Australia and the other in the United States) make allegations against more than 30 airlines, of anti-competitive conduct in relation to pricing in the air cargo business. The other two class actions (in the United States and Canada) allege that Air New Zealand together with many other airlines conspired in respect of fares and surcharges on trans-Pacific routes. All class actions are being defended.

The allegations made in relation to the air cargo business are also the subject of investigations by regulators in a number of jurisdictions including New Zealand, the United States and the European Union. A formal Statement of Objections was issued by the European Commission in 2007 to 25 airlines including Air New Zealand. Air New Zealand has responded to this Statement of Objections. On 15 December 2008 the New Zealand Commerce Commission filed proceedings against 13 airlines including Air New Zealand alleging breaches of the Commerce Act 1986. Air New Zealand is defending each of these proceedings.

In the event that a court determined, or it was agreed with a regulator, that Air New Zealand had breached relevant laws, the company would have potential liability for pecuniary penalties and to third-party damages under the laws of the relevant jurisdictions.

Environmental liabilities

Under common law and various statutes, the Crown may have responsibility to remedy adverse effects on the environment arising from Crown activities.

Departments managing significant Crown properties have implemented systems to identify, monitor and assess potential contaminated sites.

In accordance with NZ IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* any contaminated sites for which costs can be reliably measured have been included in the statement of financial position as provisions.

Kordia Group Limited

As part of its contractual obligations with clients, Kordia Group Limited has an undertaking to provide services at a certain level and should this not be achieved, Kordia Group Limited may be liable for contract penalties. It is not possible to quantify what these may be until an event has occurred. The company does not expect any liabilities to occur as a result of these contractual obligations.

The company makes advances to its subsidiary companies. The company's loan facility comprises a syndicated revolving cash advance facility between three banks, committed to a maximum amount of \$135 million (31 October 2009: \$136 million). The facility is supported by a negative pledge by the Company and its guaranteeing subsidiaries over their assets and undertakings. Under the negative pledge, each guaranteeing subsidiary may be liable for indebtedness incurred by the company and other guaranteeing subsidiaries. The company considers the negative pledge to be an insurance contract. Such contracts and cross guarantees are treated as a contingent liability and only recognised as a liability if a payment is probable.

Maui contracts

Contracts in respect of which the Crown purchases gas from Maui Mining companies and sells gas downstream to Contact Energy Limited, Vector Gas Limited and Methanex Waitara Valley Limited provide for invoices to be re-opened in certain circumstances within two years of their issue date as a result of revisions to indices. These revisions may result in the Crown refunding monies or receiving monies from those parties.

Rugby New Zealand 2011 Limited – joint venture arrangement

The Crown has agreed in joint venture arrangements with the New Zealand Rugby Union (NZRU) to an uncapped underwrite of the costs of hosting the 2011 Rugby World Cup, on a loss sharing basis (Crown 67%, NZRU 33%). A provision for the forecast losses has been made in the Government's financial statements.

The Crown has agreed to reimburse New Zealand income tax that might be incurred by the joint venture entity (Rugby New Zealand 2011 Limited) or the NZRU in relation to the joint venture entity, and has also agreed to reimburse the NZRU for New Zealand withholding tax that might be incurred on certain payments made in relation to the tournament.

The Crown has further agreed to review its level of support to the tournament if the actual tax revenue arising from the tournament exceeds forecasts.

Television New Zealand Limited

The company is subject to a number of legal claims. Given the stage of proceedings and uncertainty as to outcomes of the cases, no estimate of the financial effect can be made and no provision for any potential liability has been made in the financial statements.

Treaty of Waitangi claims

Under the Treaty of Waitangi Act 1975, any Māori may lodge claims relating to land or actions counter to the principles of the Treaty with the Waitangi Tribunal. Where the Tribunal finds a claim is well founded, it may recommend to the Crown that action be taken to compensate those affected. The Tribunal can make recommendations that are binding on the Crown with respect to land that has been transferred by the Crown to an SOE or tertiary institution, or is subject to the Crown Forest Assets Act 1989.

Treaty of Waitangi claims – settlement relativity payments

The Deeds of Settlement negotiated with Waikato-Tainui and Ngāi Tahu include a relativity mechanism. The mechanism provides that, where the total redress amount for all historical Treaty settlements exceeds \$1 billion in 1994 present-value terms, the Crown is liable to make payments to maintain the real value of Ngāi Tahu's and Waikato-Tainui's settlements as a proportion of all Treaty settlements. The agreed relativity proportions are 17% for Waikato-Tainui and approximately 16% for Ngāi Tahu. The non-quantifiable contingent liability relates to the risk that total settlement redress, including binding recommendations from the Waitangi Tribunal, will trigger these relativity payments.

Westpac Banking Corporation

Under the Domestic Transaction Banking Services Master Agreement with Westpac Banking Corporation, dated 30 November 2004, the Crown has indemnified Westpac:

- in relation to letters of credit issued on behalf of the Crown, and
- for costs and expenses incurred by reason of third-party claims against Westpac relating to indirect instructions, direct debits, third-party cheques, departmental credit card merchant agreements, use of online banking products and IRD processing arrangements.

Other contingencies

Foreshore and seabed

The Foreshore and Seabed Act 2004 (FSA):

- vests the full legal and beneficial ownership of the public foreshore and seabed in the Crown
- provides for the recognition and protection of ongoing customary rights with respect to the public foreshore and seabed
- enables applications to the High Court to investigate if previously held common law rights have been adversely impacted, and if so, providing for those affected either to participate in the administration of a foreshore and seabed reserve or else enter into formal discussions on redress, and

- provides for general rights of public access and recreation in, on, over and across the public foreshore and seabed and general rights of navigation within the foreshore and seabed.

The public foreshore and seabed means the marine area that is bounded on the landward side by the line of mean high water springs; and on the seaward side by the outer limits of the territorial sea, but does not include land subject to a specified freehold interest (refer section 5 of the FSA).

The FSA provides for the Crown to hold the public foreshore and seabed, as its absolute owner, on behalf of the public of New Zealand. Because of the complex nature of the Crown's ownership interest in the public foreshore and seabed and because we are unable to obtain a reliable valuation of the Crown's interest, the public foreshore and seabed has not been recognised as an asset in these financial statements.

Quantifiable contingent assets

Contingent assets are potential assets dependent on a particular event occurring. As at 31 March 2010, the Crown held quantifiable contingent assets totalling \$274 million (\$1,563 million at 31 October 2009).

The major components being:

Inland Revenue – legal proceedings and disputes

Legal proceedings and disputes are contingent assets in relation to Inland Revenue pending assessments. Contingent assets arise where Inland Revenue has advised a taxpayer of a proposed adjustment to their tax assessment. There has been no amended assessment issued at this point or revenue recognised so these are recorded as legal proceedings and disputes – tax. The taxpayer has the right to dispute this adjustment and a disputes resolution process is entered into. Inland Revenue quantifies a contingent asset based on the likely outcome of the disputes process based on experience and similar prior cases.

The reduction in contingent assets is owing to potential interest receivable on the dispute with a number of financial institutions regarding the tax treatment of certain structured finance transactions, which has now been settled.

\$199 million at 31 March 2010 (\$1,488 million at 31 October 2009)

Ministry of Education – suspensory loans

Suspensory loans issued by the Minister of Education to integrated schools.

\$66 million at 31 March 2010 (\$69 million at 31 October 2009)