4

Specific Fiscal Risks

The Statement of Specific Fiscal Risks is required by the Public Finance Act 1989 to set out, to the fullest extent possible, all government decisions and other circumstances known to the Government at the date of the finalisation of the fiscal forecasts that may have a material effect on the fiscal and economic outlook, but are not certain enough in timing or amount to include in the fiscal forecasts. Although the process for disclosure of specific fiscal risks involves a number of parties, including government departments, the Treasury and the Minister of Finance, there remains a possibility that not every risk is identified. Disclosure of known risks is also subject to specific requirements and materiality thresholds, which are described after the Statement of Specific Fiscal Risks.

Overview

Specific fiscal risks can be positive or negative and can affect revenue or spending. The links between external events and spending are indirect because new policies that change spending and revenue usually require a decision by the Government and approval from Parliament. The approach taken in this chapter is to disclose those potential policy decisions and key areas of uncertainty that may have a material effect on the fiscal outlook.

The Government generally sets aside allowances of new funding for future Budgets to manage uncertainty and cost pressures. These allowances are included in the fiscal forecasts. Current fiscal management policy is for future policy decisions affecting expenses or capital expenditure to be met through reprioritisation or from within existing provisions included in the fiscal forecasts. Future policy decisions are risks to the fiscal forecasts only to the extent that they cannot be managed from within:

- for operating expenditure, existing baselines or Budget allowances, or
- for capital expenditure, the Crown balance sheet, including the Future Investment Fund (FIF)/capital allowance.

Notwithstanding this, known material policy risks are identified as specific fiscal risks, even though the Government has more control in managing such risks through reprioritisation, the existing Crown balance sheet and the Budget allowances. This is done to ensure a prudent approach to the disclosure of risks, improve transparency and not pre-judge future decisions by governments.

The specific fiscal risks are categorised into:

- **Potential policy decisions affecting revenue:** For example, changes to tax policy or ACC levies could reduce or increase government income.
- **Potential policy decisions affecting expenses (expected to be funded from reprioritisation or Budget allowances):** Costs of policy proposals could increase or decrease expenses depending on decisions taken, and they are risks to the fiscal forecasts only to the extent that they cannot be managed within existing baselines or Budget allowances.
- **Potential capital decisions (expected to be funded from the Crown balance sheet, including the FIF/capital allowance):** Capital investment decisions are risks to the fiscal forecasts only to the extent that they cannot be managed within the Crown balance sheet, including the FIF/capital allowance.
- **Matters dependent on external factors:** The Crown's liability for costs is sometimes dependent on external factors such as the outcome of negotiations or international obligations.

A range of generic risks to the fiscal forecasts are not recognised as specific fiscal risks:

- The most significant economic risks have been identified in Chapter 3.
- Business risks and volatility in the returns from the Crown's investments relating to the broader economic and commercial environment.
- General cost pressures, such as those associated with demographic changes (eg, an ageing population).
- Potential risks from changes in demand for government services or transfer payments owing to underlying structural factors (such as changes in demand for Jobseeker Support).
- The costs of future individual natural disasters, and other major events, as they usually occur infrequently and their occurrence, nature and timing cannot be predicted. Once a disaster does occur, a number of choices arise about how to respond and when potential liabilities are recognised (eg, through setting aside an allocation of funding). Specific risks are disclosed at this point based on the range of possible responses.

The final part of the chapter contains a current list of contingent liabilities and contingent assets. Contingent liabilities are costs that the Crown will have to face if a particular event occurs or are present liabilities that are unable to be measured. Typically, contingent liabilities consist of guarantees and indemnities, legal disputes and claims on uncalled capital. The largest quantified contingent liabilities are to international financial organisations and mostly relate to uncalled capital and promissory notes. Contingent assets are possible assets that have arisen from past events but the value of the asset, or whether it will eventuate, will not be confirmed until a particular event occurs.

Statement of Specific Fiscal Risks

Summary Table

The matters listed below are disclosed as specific fiscal risks because they meet the rules for disclosure outlined after this Statement. Full descriptions of the risks listed below are set out in the next section. Where quantification is possible, this is included in the description of the risk.

Specific fiscal risks as at 29 April 2014	**Status**[9]
Potential policy decisions affecting revenue	
ACC – Funding Policy Review	Unchanged
Revenue – Income-sharing Tax Credits	Unchanged
Services Funded by Third Parties	Unchanged
Potential policy decisions affecting expenses (expected to be funded from reprioritisation or Budget allowances)	
ACC – Work-related Gradual Process Disease and Infection	Unchanged
Budget Operating Initiatives	Changed
Canterbury Earthquake Recovery – Christchurch Central Recovery Plan	Unchanged
Christchurch City Council/Crown Cost Sharing	Unchanged
Communications – Ultra-Fast Broadband Initiative	Unchanged
Defence Force – Operating and Capital Costs	New
Finance – Concessionary Loans	New
Government Response to Wai 262	Unchanged
Housing – Reform of Social Housing	Unchanged
Revenue – KiwiSaver Auto-enrolment	Changed
Revenue – Transformation and Technology Renewal	Unchanged
Social Development – Vulnerable Children White Paper	Changed
Social Development – Welfare Reform Costs	Changed
Social Development – Welfare Reform Forecast Benefit Savings	Unchanged
State Sector Employment Agreements	Unchanged
Potential capital decisions (expected to be funded from the Crown balance sheet, including the FIF/capital allowance)	
Departmental Capital Intentions	Changed
Earthquake Strengthening for Crown-owned Buildings	Unchanged
Finance – Crown Overseas Properties	Unchanged
Primary Industries – Investment in Water Infrastructure	Unchanged
Transport – Auckland Transport Projects	Changed
Transport – Support for KiwiRail	Changed

9 *Unchanged* – risks that have not substantively changed since the previous *Economic and Fiscal Update*.
Changed – risks that have changed substantively from the previous *Economic and Fiscal Update*.
New – risks that have not been disclosed in the previous *Economic and Fiscal Update*.

Specific fiscal risks as at 29 April 2014	Status[9]
Matters dependent on external factors	
ACC – Levies	Unchanged
ACC – Non-earners' Account	Unchanged
Canterbury Earthquake Recovery – Residential Red Zone	Unchanged
Caregiver Employment Conditions	New
Communications – Potential Impairment in Value of Broadband Investment	Unchanged
Defence Force – Potential Rationalisation, Revaluation and Disposal of NZDF Assets	Unchanged
Energy – Crown Revenue from Petroleum Royalties	Unchanged
Finance – EQC	Unchanged
Finance – Goodwill on Acquisition	Unchanged
Finance – Solid Energy	New
Finance – Southern Response Earthquake Services Support	Unchanged
Housing – Divestment of Housing	Unchanged
Revenue – Cash Held in Tax Pools	Unchanged
Revenue – Student Loans	New
Treaty Negotiations – Treaty Settlement Forecasts	Unchanged
Treaty Negotiations – Relativity Clause	Unchanged

Potential Policy Decisions Affecting Revenue

ACC – Funding Policy Review (Unchanged)

The Government is undertaking a review of ACC's funding policy. Adopting a lower funding target band midpoint would result in a reduction in levies and reduce Crown revenue and Crown assets, with a flow-on impact to the operating balance.

Revenue – Income-sharing Tax Credits (Unchanged)

The Government has introduced legislation to establish an income-sharing tax credit. If passed as introduced, the legislation will allow couples with children under the age of 18 to pool their earnings for income tax purposes if they meet certain criteria. If implemented, the changes could reduce tax revenue by $500 million a year once the scheme is fully operational. The Finance and Expenditure Committee has recommended that the significant fiscal cost of the package be addressed before the Bill proceeds further.

Services Funded by Third Parties (Unchanged)

A wide range of government services are funded through third party fees and charges. Demand for these services can vary with a direct impact on revenue received. There is a risk the Government may need to provide additional funding if revenue collected is lower than the total costs of providing the services. There is also a risk that changes will be required to the way government services are delivered, which could result in costs to the Crown.

Potential Policy Decisions Affecting Expenses (Expected to be Funded from Reprioritisation or Budget Allowances)

ACC – Work-related Gradual Process Disease and Infection (Unchanged)

Under current legislation, the Government incurs an obligation for Work-related Gradual Process Disease and Infection claims when the claim is made, and an expense is recognised at this point. The liability for commercial accident and sickness insurance contracts would usually be recognised when exposure to conditions that will give rise to a claim occurs. An amendment to legislation would be required to recognise claims at the same time as for commercial contracts. This is under active consideration, but would require an appropriate legislative vehicle. An initial adjustment to the liability, and an expense of about $650 million would need to be reported if such an amendment were to be made.

Budget Operating Initiatives (Changed)

Future Budgets may well include new operating initiatives other than those identified in other specific fiscal risks. Such new operating initiatives are risks to the fiscal forecasts only to the extent they cannot be managed through reprioritisation or from within the existing provision in the fiscal forecasts for forecast new operating spending. The Government's stated intention is that all new operating initiatives will be managed through these mechanisms.

Canterbury Earthquake Recovery – Christchurch Central Recovery Plan (Unchanged)

The Crown is partially funding the construction of Anchor Projects as part of the Christchurch Central Recovery Plan as set out in the cost-sharing agreement with the Christchurch City Council. The extent of funding will vary from project to project, dependent on final project costs. Business cases are progressing through the decision-making process. Project costing for construction of the Anchor Projects will become increasingly clear during the business case process and the subsequent procurement phase. The Crown's contribution may differ from that included in the fiscal forecasts.

Christchurch City Council/Crown Cost Sharing (Unchanged)

The Crown is partially funding the recovery of local infrastructure in Canterbury as set out in the cost-sharing agreement with the Christchurch City Council. The agreement includes a review clause. The review is to be completed by 1 December 2014. Therefore, the fiscal forecasts make no allowance for additional costs arising from the review.

Communications – Ultra-Fast Broadband Initiative (Unchanged)

The Government has expressed support for Crown Fibre Holdings to enter into discussions with Chorus Limited to help manage potential issues for Chorus in delivering the Ultra-Fast Broadband Initiative. Depending on their nature, the outcomes of those discussions could give rise to a fiscal risk. The Government's expectation is that any options arising from the discussions will remain within the current funding envelope.

Defence Force – Operating and Capital Costs (New)

Operating and capital investment decisions may be made to achieve Defence White Paper (2010) policy over the forecast period. In 2013, the Government reconsidered New Zealand Defence Force (NZDF) funding, output requirements and capability intentions, through the Defence Mid-Point Rebalancing Review. The Government is yet to make final decisions on future funding for NZDF. However, funding increases may be approved for NZDF within the forecast period.

Finance – Concessionary Loans (New)

The Crown has provided loans to local government and iwi-based organisations on a concessionary, usually interest free, basis to achieve public policy purposes. To reflect the concession, these loans have been written down and are measured at $290 million in the financial statements. There is, however, a risk that the write-down provisions may be insufficient to cover the credit risk involved in these non-commercial loans.

Government Response to Wai 262 (Unchanged)

The Waitangi Tribunal's report on the Wai 262 claim focuses on the protection of Māori culture and identity, with a particular focus on mātauranga Māori and associated taonga. The Tribunal's recommendations are directed towards a number of government agencies individually, as groups and across sectors. The Government has yet to respond to the Tribunal's report and recommendations.

Housing – Reform of Social Housing (Unchanged)

The Government has decided to change the policy settings for social housing. This includes growing third party providers of social housing, increasing the effectiveness of financial assistance, and Housing New Zealand Corporation focusing on providing social housing to those with the greatest housing need. Increasing the scale or speed of change may require reprioritisation or additional funding.

Revenue – KiwiSaver Auto-enrolment (Changed)

The Government has announced its intention to consult on the design of a one-off KiwiSaver auto-enrolment exercise to increase the number of KiwiSaver members. The Government will proceed with a one-off KiwiSaver enrolment exercise only when it is confident that such a step poses no significant risks to returning to, and maintaining, an operating surplus and debt repayment is on track. An auto-enrolment exercise is likely to entail a one-off cost for kick-start payments to new members and ongoing additional costs for the Member Tax Credit. Depending on the timing, design features and take-up rate, these costs could be in the order of $100 million to $290 million over the first four years after auto-enrolment takes place, and are expected to be funded out of the operating allowance.

Revenue – Transformation and Technology Renewal (Unchanged)

The Government is exploring options that will change the way Inland Revenue manages its processes and data. Any changes could impact tax revenue collections and may have material costs to implement. Inland Revenue has commenced the development of a detailed business cases for Stage 1: Enabling secure digital services. The business cases will inform the Government's decision-making for the first stage of transformation and may require significant reprioritisation or new funding.

Social Development – Vulnerable Children White Paper (Changed)

The Government has begun to implement proposals to better identify and provide assistance to vulnerable children. While funding for 2014/15 has been included in the fiscal forecasts, future costs of the proposal are still being developed. To the extent that these cannot be funded from reprioritisation, additional funding from the Budget operating allowance may be required.

Social Development – Welfare Reform Costs (Changed)

The Welfare Reform package of changes to the benefit system was introduced from July 2013, following amendments to the Social Security Act 1964. The current phase is to review programmes with a view to reducing future benefit dependency and long-term liability. Additional funding was appropriated at Budget 2014. The extent of any further costs associated with the ongoing implementation of the Investment Approach is uncertain.

Social Development – Welfare Reform Forecast Benefit Savings (Unchanged)

A conservative estimate of the likely benefits from Welfare Reform has been included in the fiscal forecasts. The actual impact may differ owing to behavioural factors and the complexity in implementing the reforms, with a corresponding impact on benefit expenditure.

State Sector Employment Agreements (Unchanged)

A number of large collective agreements are due to be negotiated 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 of restraint given its current fiscal stance and that agreements will be managed within the current fiscal forecasts.

Potential Capital Decisions (Expected to be Funded from the Crown Balance Sheet, Including the FIF/Capital Allowance)

Departmental Capital Intentions (Changed)

Future Budgets may well include new capital initiatives other than those identified in other specific fiscal risks. Such initiatives are likely to be primarily from the 16 capital-intensive agencies or sectors that are required to identify their capital spending intentions over the next 10 years based on current policy settings and certain demographic and inflation assumptions. The Government expects that these intentions will be managed back through a range of measures such as prioritisation, changes to asset utilisation, alternative methods of service delivery and changes to policy settings. New capital initiatives and departmental capital intentions are risks to the fiscal forecasts only to the extent they cannot be managed through existing balance sheets, including the FIF, and the provision in the fiscal forecasts for forecast new capital spending.

Earthquake Strengthening for Crown-owned Buildings (Unchanged)

There is a possibility that the Crown will incur costs for earthquake strengthening some of its buildings that do not meet modern building standards. The Government is currently undertaking a stocktake of Crown-owned earthquake-prone buildings. The likelihood, timing and fiscal impact of any earthquake strengthening are uncertain.

Finance – Crown Overseas Properties (Unchanged)

The Government holds New Zealand House in London on a long-term lease from the Crown Estate (UK). Depending on the outcome of ongoing discussions with the Crown Estate an upgrade to the building may be required. A rough-order cost estimate for this upgrade is $100 million over the forecast period.

Primary Industries – Investment in Water Infrastructure (Unchanged)

In addition to $80 million provided in Budget 2013 and $40 million provided in Budget 2014, the Government will consider providing up to $280 million in future Budgets to Crown Irrigation Investments Limited as schemes reach the "investment-ready" stage.

Transport – Auckland Transport Projects (Changed)

The Government has signalled its intention to accelerate transport projects in the Auckland Council's Auckland Plan, including Auckland Manukau Eastern Transport Initiatives, the East-West Link and support for the City Rail Link and a second Waitemata Harbour Crossing. Decisions on further Crown financial assistance for Auckland Manukau Eastern Transport Initiatives and the East-West Link will be made as part of future Budgets.

Transport – Support for KiwiRail (Changed)

The Government has supported KiwiRail Holdings Limited (KiwiRail) with around $1 billion invested in its plan to become a commercially viable network in Budgets 2010 to 2014. Further funding is being sought by KiwiRail in support of this objective. A major review of the business has commenced and will be assessed to inform Budget 2015 and any further investment.

Matters Dependent on External Factors

ACC – Levies (Unchanged)

Revenue from the levies set for the Work, Earners' and Motor Vehicle accounts may be more or less than is required to cover the cost of claims, if factors such as claims experience, ACC performance and economic assumptions (particularly discount rates) turn out differently from what has been forecast. Any such variance will have a corresponding impact on the operating balance.

ACC – Non-earners' Account (Unchanged)

The amount of funding provided by the Crown (and included in the fiscal forecasts) for the Non-earners' Account may be more or less than is required to cover the cost of claims, if factors such as claims experience, ACC performance and economic assumptions (particularly discount rates) turn out differently from what has been forecast. Any such variance will have a corresponding fiscal impact.

Canterbury Earthquake Recovery – Residential Red Zone (Unchanged)

Some recoveries from the EQC and private insurers remain outstanding and there is a risk that final recoveries may be greater or less than forecast. In addition, potential costs associated with the future use of residential red zone are uncertain. The future value may change depending on any future alternate uses of the land.

Caregiver Employment Conditions (New)

Several cases and funding claims in the disability support and aged care sectors may involve significant costs to the Crown relating to interpretation of the Minimum Wage Act 1983, the Equal Pay Act 1972 and the Government's policy of paying certain family members through its Funded Care Policy. Changes to the existing policy could require additional funding. Successful litigation may have implications for agencies that target assistance based on family circumstances and/or employ workers under similar contracts.

Communications – Potential Impairment in Value of Broadband Investment (Unchanged)

The Government has set aside $1.345 billion to progressively capitalise Crown Fibre Holdings so that it can invest with private partners in a new network delivering "ultra-fast" broadband services. Given the contracts entered into, the extent of the recovery of this investment is particularly dependent on the number of connections made to the network. The fiscal forecasts include a provision for impairing this investment, but the final amount of the impairment may vary from this provision.

Defence Force – Potential Rationalisation, Revaluation and Disposal of NZDF Assets (Unchanged)

The Government is considering the potential to dispose of a number of NZDF assets, including the Seasprite helicopters and Unimog trucks. Depending on market conditions, the timing of disposal and sale price received could have an impact on the Government's overall financial position. NZDF is also completing analysis of inventory that is surplus to requirements and is over and above the existing provision for obsolescence. The existing provision is also being reviewed to ensure that all items comprising the provision are still relevant.

Energy – Crown Revenue from Petroleum Royalties (Unchanged)

Crown revenue from petroleum royalties is very dependent upon extraction rates, the US dollar value per barrel and the US dollar/NZ dollar exchange rate. Movements up or down in either of these variables could result in a significant decrease or increase in Crown revenue. The overall impact for the Crown could be positive or negative.

Finance – EQC (Unchanged)

The net financial position of EQC, and the size of any requirement for additional Crown funding, remain uncertain, although EQC expects the National Disaster Fund to be fully depleted during the 2014/15 financial year, after which the Crown funding will begin. The uncertainty is around EQC's outstanding claims liability – the actuarial estimate of EQC's outstanding claims liability is highly uncertain and sensitive to assumptions; for example, construction demand surge, land damage estimates, legal challenges, reinsurance recoveries and the profile of claims settlement. The magnitude of the net outstanding cost claims is large, so small percentage changes in the liability can have a material impact on the fiscal forecasts.

Finance – Goodwill on Acquisition (Unchanged)

As at 30 June 2013, the Government had goodwill on acquisition of a number of sub-entities totalling $655 million. Under New Zealand accounting standards (NZIAS 36), such goodwill items are required to be assessed annually for impairment. If there is any indication that the goodwill may be impaired, the recoverable amount of the cash generating units to which the goodwill is allocated is required to be estimated. If the recoverable amount is less than the carrying amount of those units, the units and the goodwill allocated to them are regarded as impaired and the Government is required to recognise impairment losses in the operating statement. Such assessments will be conducted at the end of the financial year, and the fiscal forecasts currently make no allowance for such impairment losses.

Finance – Solid Energy (New)

Since Solid Energy's financial restructure in October 2013 the company's export prices have deteriorated significantly driven mainly by a decrease in US dollar coal price. The company continues to develop and implement a business strategy to adapt to these challenging market conditions and continue operating. Any changes to the restructure arrangements or further deterioration in market conditions or the company's financial position may adversely impact the Crown.

Finance – Southern Response Earthquake Services Support (Unchanged)

The ultimate cost to the Crown of settling earthquake claims remains subject to significant uncertainty. Out-year forecasts assume that the actual cost to settle claims will align with the actuary's central estimate of the claims provision. There is a risk that the actual cost could vary from this estimate.

Housing – Divestment of Housing (Unchanged)

The forecasts reflect related divestments and redevelopments of some housing property. Property sales are subject to market conditions and therefore there is an inherent level of uncertainty about the return to the Crown associated with forecast divestments and to the proposed funding of the related developments.

Revenue – Cash Held in Tax Pools (Unchanged)

Funds held in tax pools are recognised as a Crown asset. There is a risk that funds held in these pools, over and above a taxpayer's provisional tax liability, may be withdrawn by that taxpayer, resulting in a reduction in the Crown's available cash reserves.

Revenue – Student Loans (New)

The valuation of student loans in the fiscal forecasts use data compiled by Statistics New Zealand from the Ministry of Social Development, Ministry of Education and Inland Revenue. The structure of the datasets has changed to those previously used. While this change is expected to improve the accuracy of the forecasts in the future, the change may lead to revisions of assumptions in the short term which could affect the valuation of outstanding student loans.

Treaty Negotiations – Treaty Settlement Forecasts (Unchanged)

The fiscal forecasts include provision for the cost of future Treaty settlements. Given settlements are finalised through negotiations; there is a risk that the timing and amount of the settlements could differ from the profile included in the fiscal forecasts.

Treaty Negotiations – Relativity Clause (Unchanged)

The Deeds of Settlement negotiated with Waikato-Tainui and Ngāi Tahu include a relativity mechanism. Now that the total redress amount for all historical Treaty settlements exceeds $1 billion in 1994 present-value terms, the mechanism provides that the Crown is liable to make payments to maintain the real value of Ngāi Tahu 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.

There is a risk that the timing and amount of the expense for the relativity payments may differ from that included in the fiscal forecasts. There is also uncertainty on how various disputes concerning the interpretation of the mechanism will be resolved.

Risks Removed Since the 2013 *Half Year Update*

The following risks have been removed since the 2013 *Half Year Update*:

Expired risks	Reason
Defence Force – Mid-point Rebalancing Review	Merged with Defence Force – Operating and Capital Costs risk
Environment – Post-2012 International Climate Change Obligations	No longer material
Health – Litigation in the Disability Support and Aged Care Areas	Merged with Caregiver Employment Conditions risk
Justice – Christchurch Justice and Emergency Services Precinct	No longer material
Finance – Government Commitments to International Financial Institutions	No longer material
Finance – Sale of Part of the Crown's Shareholding in Certain Companies	Included in forecasts

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

The Public Finance Act 1989 requires that the Statement of Specific Fiscal Risks sets out all government decisions, contingent liabilities or contractual obligations known to the Government and subject to specific requirements that may have a material effect on the economic or fiscal outlook.[10]

The criteria and rules set out below are used to determine if government decisions or other circumstances should 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 the following criteria:

- 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 probable[11] the matter will be approved, or it is reasonably probable the situation will occur.

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[10] The Statement of Specific Fiscal Risks is a requirement set out in sections 26Q and 26U of the Public Finance Act 1989.

[11] 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).

Additionally, any other matters may be incorporated into the forecasts if the Secretary to the Treasury considers, using 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.

Rules for the Disclosure of Specific Fiscal Risks

Matters are disclosed as specific fiscal risks if:

- the likely impact is more than $100 million over five years, and either
- a decision has not yet been taken but it is reasonably possible[12] (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 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 best professional judgement, that the matters may have a material effect (more than $100 million over five years) 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 criterion (ie, are less than $100 million over five years), or if they are unlikely[13] to be approved or occur within the forecasting period.

Additionally, the Minister of Finance may determine that a matter be 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.

If possible, the Minister of Finance should avoid withholding the matter, either by making a decision on it before the forecasts are finalised, or by disclosing it without quantifying the risk.

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[12] 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).

[13] 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).

Contingent Liabilities and Contingent Assets

Contingent liabilities are possible costs that have arisen from past events, but the amount of the liability, or whether it will eventuate, will not be confirmed until a particular event occurs or present liabilities that are unable to be measured with sufficient reliability to be recorded in the financial statements (unquantifiable liabilities).

Typically, contingent liabilities consist of guarantees and indemnities, uncalled capital and legal disputes and claims. 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, or the amount becomes sufficiently reliable to record as a liability, it would reduce the operating balance and net worth and increase debt. In the case of contingencies for uncalled capital, the negative impact would be restricted to core Crown net debt because the cost would be offset by the acquisition of capital.

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 possible assets that have arisen from past events but the amount of the asset, or whether it will eventuate, will not be confirmed until a particular event occurs.

Only contingent liabilities and contingent assets involving amounts of over $100 million are separately disclosed. Quantifiable contingencies less than $100 million are aggregated in the “other quantifiable” total.

Some contingencies of the Crown are not able to be quantified. We have disclosed all unquantifiable contingent liabilities and unquantifiable contingent assets that are not expected to be remote.[14]

Contingent liabilities have been stated as at 31 March 2014, being the latest set of reported contingent liabilities.

[14] Remote is defined as being an item with less than a 10% chance of occurring.

Quantifiable Contingent Liabilities and Contingent Assets

Contingent liabilities		
	Status[15]	**($millions)**
Guarantees and indemnities		
Other guarantees and indemnities	Unchanged	158
		158
Uncalled capital		
Asian Development Bank	Unchanged	2,763
International Monetary Fund – promissory notes	Unchanged	1,033
International Bank for Reconstruction and Development	Unchanged	948
International Monetary Fund – arrangements to borrow	Unchanged	972
Other uncalled capital	Unchanged	22
		5,738
Legal proceedings and disputes		
Tax disputes	Unchanged	591
Other legal proceedings and disputes	Unchanged	65
		656
Other quantifiable contingent liabilities		
Unclaimed monies	Unchanged	112
Transpower New Zealand Limited	Unchanged	150
Other quantifiable contingent liabilities	Unchanged	228
		490
Total quantifiable contingent liabilities		**7,042**
Contingent assets		
Tax disputes	Unchanged	118
Other quantifiable contingent assets	Unchanged	46
Total quantifiable contingent assets		**168**

15 Status of contingent liabilities or assets when compared to the *Half Year Economic and Fiscal Update* published on 17 December 2013.

Unquantifiable Contingent Liabilities and Contingent Assets

Contingent liabilities	
Indemnities:	**Status**
Air New Zealand	Unchanged
Contact Energy Limited	Unchanged
Earthquake Commission (EQC)	Unchanged
Genesis Energy Limited	Unchanged
Housing New Zealand Corporation	Unchanged
Justices of the Peace, Community Magistrates and Disputes Tribunal Referees	Unchanged
Maui Contracts	Unchanged
Maui Partners	Unchanged
New Zealand Aluminium Smelter and Comalco	Unchanged
New Zealand Local Authorities	Unchanged
New Zealand Railways Corporation	Unchanged
Persons exercising investigating powers	Unchanged
Synfuels-Waitara Outfall Indemnity	Unchanged
Westpac New Zealand Limited	Unchanged
Legal claims and proceedings:	
Accident Compensation Corporation (ACC) litigations	Unchanged
Air New Zealand litigation	Unchanged
Television New Zealand	Unchanged
Treaty of Waitangi claims	Unchanged
Ministry of Education litigation	Unchanged
Other unquantifiable contingent liabilities:	
Criminal Proceeds (Recovery) Act 2009	Unchanged
Environmental liabilities	Unchanged
Treaty of Waitangi claims – settlement relativity payments	Unchanged

The following unquantifiable contingent liability was removed: Meridian Energy Limited Initial Public Offering.

Description of Contingent Liabilities

Quantifiable contingent liabilities over $100 million

Uncalled capital

As part of the Crown's commitment to a multilateral approach to ensure global financial and economic stability, New Zealand, as a member country of these organisations, contributes capital by subscribing to shares in certain institutions.

The capital (when called) is typically used to raise additional funding for loans to member countries or, in the case of the quota contributions, to directly finance lending to members. For New Zealand and other donor countries, capital contributions comprise both "paid in" capital and "callable capital or promissory notes".

The Crown's uncalled capital subscriptions over $100 million are as follows:

Uncalled capital	**31 March 2014**	**30 June 2013**
	$millions	**$millions**
Asian Development Bank	2,763	2,992
International Monetary Fund – promissory notes	1,033	1,163
International Bank for Reconstruction and Development	948	1,056
International Monetary Fund – arrangements to borrow	972	1,052

Legal proceedings and disputes

Tax in dispute

When a taxpayer disagrees with an amended 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 contingent liability represents the maximum liability Inland Revenue has in respect of these cases.

$591 million at 31 March 2014 ($641 million at 30 June 2013)

Other quantifiable contingent liabilities

Unclaimed monies

Under the Unclaimed Money Act 1971, entities (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.

$112 million at 31 March 2014 ($101 million at 30 June 2013)

Transpower New Zealand Limited

Transpower has a contingent liability relating to excess capital expenditure on the North Island Grid Upgrade Project (NIGU). The NIGU spend exceeds the amount initially approved in 2006. If the excess expenditure is not approved by the Commerce Commission it cannot be recovered from customers. NIGU is operational and a submission for the excess expenditure has been made.

$150 million at 31 March 2014 ($156 million at 30 June 2013)

Unquantifiable contingent liabilities

This part of the Statement provides details of those contingent liabilities of the Crown that are not quantified, excluding those that are considered remote, reported by the following categories:

a Indemnities.

b Legal disputes.

c Other contingent liabilities.

a Indemnities

Indemnities are legally binding promises where the Crown undertakes to accept the risk of loss or damage that another party may suffer or to hold the other party harmless against loss caused by a specific stated event.

A number of these indemnities are provided to organisations within the Crown's control. If these indemnities were to crystallise, the Crown would compensate the individual entity for the loss and there would likely be an adverse impact on core Crown expenses and core Crown net debt.

Party indemnified	**Instrument of indemnification**	**Actions indemnified**
Air New Zealand	Deed of indemnity issued 24 September 2001.	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.
Contact Energy Limited	The Crown and Contact Energy signed a number of documents to settle in full Contact's outstanding land rights and geothermal asset rights at Wairakei.	The documents contained two reciprocal indemnities between the Crown and Contact to address the risk of certain losses to the respective parties' assets arising from the negligence or fault of the other party.
Earthquake Commission (EQC)	Section 16 of the Earthquake Commission Act 1993.	As set out in the Earthquake Commission Act 1993, the Crown shall fund any deficiency in EQC's assets to cover its financial liabilities on such terms and conditions that the Minister of Finance determines. See risk page 71.
Genesis Energy Limited	Deed between Genesis Power Limited and the Crown.	The agreement sees the Crown compensate Genesis in the event that Genesis has less gas than it requires for the long-term supply of gas to cover Huntly Power station's minimum needs.
	Genesis acquisition of Tekapo A & B power stations.	Indemnity against any damage to bed of lakes and rivers subject to operating easements.

Party indemnified	Instrument of indemnification	Actions indemnified
Housing New Zealand Corporation (HNZC)	The Crown has provided a warranty in respect of title to the assets transferred to Housing New Zealand Limited (HNZL).	The Crown indemnified HNZL against: • any breach of the warranty provided, and • any third party claims that are a result of acts or omissions prior to 1 November 1992. The Crown 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.
Justices of the Peace, Community Magistrates and Disputes Tribunal Referee	Section 197 of the Summary Proceedings Act 1957. Section 58 of the Disputes Tribunal Act 1988.	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.
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.	The contracts 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.
Maui Partners	Confidentiality agreements with the Maui Partners in relation to the provision of gas reserves information.	Any losses arising from a breach of the deed.
New Zealand Aluminium Smelter and Comalco	The Minister of Finance signed indemnities in November 2003 and February 2004 in respect of aluminium dross currently stored at another site in Invercargill.	The indemnity relates to costs incurred in removing the dross and disposing of it at another site if required to do so by an appropriate authority.
New Zealand Local Authorities	Section 9 of the Civil Defence Emergency Management Act 2002. Civil Defence Emergency Management Plan.	The Guide to the National Civil Defence Emergency Management Plan ("the Guide") states that, with the approval of the Minister, the Government will reimburse local authorities, in whole or in part, for certain types of response and recovery costs incurred as a result of a local or national emergency. The Guide is approved and issued by the Director of Civil Defence Emergency Management.

Party indemnified	Instrument of indemnification	Actions indemnified
New Zealand Railways Corporation	The Minister of Finance signed the indemnity on 1 September 2004.	The directors of New Zealand Railways Corporation are indemnified against all liabilities in connection with the Corporation taking ownership and/or responsibility for the national rail network and any associated assets and liabilities.
	Section 10 of the Finance Act 1990.	The Act guarantees all loan and swap obligations of the New Zealand Railways Corporation.
Persons exercising investigating powers	Section 63 of the Corporations (Investigation and Management) Act 1989.	Indemnifies the Financial Markets Authority (formerly Securities Commission), the Registrar of Companies, every statutory manager of a corporation, every member of an advisory committee appointed under the Act and persons appointed pursuant to sections 17 to 19 of the Act (to exercise powers of inspection and investigation). The indemnity applies to the exercise, or omission to exercise, of any powers under the Act, unless the exercise of the power or the omission is shown to be in bad faith.
Synfuels-Waitara Outfall Indemnity	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 which was laid across the Waitara meat processing plant site. The Crown has the benefit of a counter indemnity from NZLFI which has since been transferred to Methanex Motunui Limited.
Westpac New Zealand Limited	The Domestic Transaction Banking Services Master Agreement with Westpac Banking Corporation (Westpac's rights and obligations under this agreement were vested in Westpac New Zealand Limited under the Westpac New Zealand Act 2006), 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.

Party indemnified	Instrument of indemnification	Actions indemnified
	Supplier Payments Service – New Zealand Government Master Agreement dated 23 June 2010.	The Crown has indemnified Westpac New Zealand Limited against certain costs, damages and losses to third parties resulting from unauthorised, forged or fraudulent payment instructions (excluding costs, damages and losses arising from Westpac's wilful default, negligence or breach of the agreement or other applicable legal obligation).

Legal claims and proceedings

Numerous legal actions have been brought against the Crown. However, in the majority of these actions it is considered a remote possibility that the Crown would lose the case, or if the Crown were to lose it would be unlikely to have greater impact than a $20 million impact. Based on these factors, not all legal actions are individually disclosed. The claims that are disclosed individually, while they cannot be quantified, have the potential to exceed $20 million in costs.

Accident Compensation Corporation (ACC) litigations

There are a number of actions involving ACC in existence, arising from the statutory review and appeal process, and in the main coming from challenges to operational decisions made by ACC. Given the nature of these proceedings and uncertainty as to their outcomes, attempting to quantify the financial effect would be unrealistic, so no estimate has been made.

Air New Zealand litigation

Air New Zealand is currently named in class actions. 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. A class action in the United States alleges that Air New Zealand together with many other airlines conspired in respect of fares and surcharges on trans-Pacific routes. The United States class action is being defended. Claims against Air New Zealand in the Australian class action are to be discontinued under terms of a proposed settlement of the proceedings. Air New Zealand is not contributing to that settlement. The allegations made in relation to the air cargo business are also the subject of proceedings by the Australian Competition and Consumer Commission. A defended hearing in the Federal Court concluded in May 2013 and a decision is awaited. In the event that the Court determines that Air New Zealand had breached Australian laws, the Company would have potential liability for pecuniary penalties.

Television New Zealand Limited (TVNZ)

In the normal course of business various legal claims have been made against TVNZ. Given the stage of proceedings and uncertainty as to the outcomes of the claims, 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 certain 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 which has been transferred by the Crown to an SOE or tertiary institution, or is subject to the Crown Forest Assets Act 1989.

On occasion, Māori claimants pursue the resolution of particular claims against the Crown through higher courts. There are currently two such actions against the Crown being heard at the Court of Appeal and the Supreme Court. Failure to successfully defend such actions may result in a liability for historical Treaty grievances in excess of that currently anticipated.

Ministry of Education litigation

Post Primary Teachers Association and several teachers have lodged a claim in the High Court alleging breach of statutory duty, and compensation, in respect of the Novopay system failures. The Ministry is defending this claim.

Other unquantifiable contingent liabilities

Criminal Proceeds (Recovery) Act 2009

The Ministry of Justice is responsible for administering the Criminal Proceeds (Recovery) Act 2009. The Act requires the Crown to give an undertaking as to damages or costs in relation to asset restraining orders. In the event that the Crown is found liable, payment may be required. The timing and amount of any possible payments required are not able to be estimated.

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.

Any contaminated sites for which costs can be reliably measured have been included in the Statement of Financial Position as provisions.

Treaty of Waitangi claims – Settlement Relativity Payments – see page 72.

Description of Contingent Assets

Quantifiable contingent assets over $100 million

Tax disputes – non-assessed

A contingent asset is recognised when Inland Revenue has advised, or was about to advise, a taxpayer of a proposed adjustment to their tax assessment. The taxpayer has the right to dispute this adjustment and a disputes resolution process can be entered into. The contingent asset is based on the likely outcome of the disputes process based on experience and similar prior cases.

$118 million at 31 March 2014 ($169 million at 30 June 2013)