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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 significant 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 or the balance sheet. 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.

Established practice is that the Government 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 allowances 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 the allowance in the fiscal forecasts for forecast new operating expenditure, or
- for capital, the existing Crown balance sheet, including the Future Investment Fund (FIF), or the allowance in the fiscal forecasts for forecast new capital spending.

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 within existing baselines, 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 the Budget operating allowance)**: 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 existing Crown balance sheet, including the FIF, or the Budget capital allowance)**: Capital investment decisions are risks to the fiscal forecasts only to the extent that they cannot be managed within the existing Crown balance sheet, including the FIF, or the Budget 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:

- Risks from changes to economic assumptions; 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 1 May 2015

Vote name (if appropriate)[13] – specific fiscal risk title	Status[14]
Potential policy decisions affecting revenue	
Labour Market – ACC Funding Policy Review	Unchanged
Revenue – Income Sharing Tax Credits	Unchanged
Revenue – Potential Tax Policy Changes	New
Services Funded by Third Parties	Unchanged
Potential policy decisions affecting expenses (expected to be funded from reprioritisation or the Budget operating allowance)	
Budget Operating Initiatives	Unchanged
Building and Housing/Social Development – Social Housing Reform	Changed
Business, Science and Innovation – Ultra-Fast Broadband Initiative	Unchanged
Canterbury Earthquake Recovery – Christchurch Central Recovery Plan – Anchor Projects	Unchanged
Christchurch City/Crown Cost Sharing – Horizontal Infrastructure	Unchanged
Concessionary Loans	Unchanged
Defence Force – Operating and Capital Costs	Unchanged
Government Response to Wai 262	Unchanged
Health – Health Benefits Limited	Unchanged
Internal Affairs – All-of-Government Common Capabilities Sustainable Funding	Unchanged
Labour Market – ACC: Work-related Gradual Process Disease and Infection	Changed
Revenue – Transformation and Technology Renewal	Unchanged
Social Development – Child, Youth and Family Modernisation	Changed
Social Development – Welfare Reform Costs	Unchanged
Social Development – Welfare Reform Forecast Benefit Savings	Unchanged
State Sector Employment Agreements	Unchanged

13 Note that some vote names have changed since the Half Year Update.

14 *Unchanged* – risks where the nature and/or scale of the risk has not changed substantively since the Half Year Update.

Changed – risks where the nature and/or scale of the risk has changed substantively since the Half Year Update.

Vote name (if appropriate)[13] – specific fiscal risk title	Status[14]
Potential capital decisions (expected to be funded from the existing Crown balance sheet, including the FIF, or the Budget capital allowance)	
Agency Capital Intentions	Unchanged
Arts, Culture & Heritage – Review of Military History Museum Arrangements	Unchanged
Earthquake Strengthening for Crown-owned Buildings	Unchanged
Finance – Asian Infrastructure Investment Bank	New
Finance – Crown Overseas Properties	Unchanged
Lands – Upgrading Landonline	New
Parliamentary Service – Parliamentary Accommodation	Unchanged
Primary Industries and Food Safety – Investment in Water Infrastructure	Unchanged
Transport – Auckland Transport Projects	Changed
Transport – Regional State Highways	Unchanged
Transport – Support for KiwiRail	Changed
Matters dependent on external factors	
Building and Housing – Divestment and Development of Housing	Changed
Business, Science and Innovation – Crown Revenue from Petroleum Royalties	Unchanged
Business, Science and Innovation – Impairment in Value of Broadband Investment	Unchanged
Canterbury Earthquake Recovery – Residential Red Zone	Unchanged
Caregiver Employment Conditions	Unchanged
Defence Force – Potential Rationalisation, Revaluation and Disposal of NZDF Assets	Unchanged
Finance – EQC	Unchanged
Finance – Goodwill on Acquisition	Unchanged
Finance – Solid Energy	Unchanged
Finance – Southern Response Earthquake Services Support	Unchanged
Labour Market – ACC levies	Unchanged
Labour Market – ACC Non-earners' Account	Unchanged
Revenue – Cash Held in Tax Pools	Unchanged
Revenue – Student Loans	Unchanged
Treaty Negotiations – Treaty Settlement Forecasts	Unchanged
Treaty Negotiations – Relativity Clause	Unchanged

Potential Policy Decisions Affecting Revenue

Labour Market – ACC Funding Policy Review (Unchanged)

The Government has reviewed ACC's funding policy and intends that there be further levy reductions across all accounts but final decisions have not yet been taken on the nature and timing of those reductions. Such reductions would reduce Crown revenue and Crown assets, with a flow-on impact to the operating balance and net worth.

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. The best estimate at the time the Bill was introduced in 2010 was that the changes will reduce tax revenues by $500 million per 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.

Revenue – Potential Tax Policy Changes (New)

Some of the items on the tax policy work programme could each have a significant positive impact on operating revenue: review of GST on goods and services purchased online, ensuring that withholding tax is paid on interest income derived from related New Zealand entities and accruing to non-residents, and work on Base Erosion and Profit Shifting including interest allocation rules and the taxation of foreign hybrid instruments and entities.

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 the Budget Operating Allowance)

Budget Operating Initiatives (Unchanged)

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.

Building and Housing/Social Development – Social Housing Reform (Changed)

The Government is progressing the Social Housing Reform Programme (SHRP). The objectives of this programme are to improve the services and assistance provided to those in housing need, building the social housing market and fully recognising the costs of the social housing system. The next stage of the programme will see work begin on Housing New Zealand Corporation (HNZC) stock transfers involving community housing organisations as well as development transactions aimed at leveraging the redevelopment potential of HNZC land and increasing the supply of social/affordable housing. Depending on the size, scope and complexity of these transactions additional funding may be required and expenses associated with these transactions will need to be accounted for.

Business, Science and Innovation – Ultra-Fast Broadband Initiative (Unchanged)

The Government's expectation is that the current funding envelope for the roll out of Ultra-Fast Broadband (UFB) phase 1 will not be breached and that the objective of rolling out UFB to 75% of New Zealanders by the end of 2019 will be met. Until the Commerce Commission issues a final decision on the pricing of the copper network, the largest partner in the roll out, Chorus, will face some degree of funding uncertainty which could give rise to a fiscal risk in achieving these targets.

Canterbury Earthquake Recovery – Christchurch Central Recovery Plan – Anchor Projects (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 scope, ownership decisions, implementation and project costs, and will to some extent eventually be recovered. Business cases are progressing through the decision-making process and construction costs 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/Crown Cost Sharing – Horizontal Infrastructure (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 yet to be completed, so the Crown cannot yet consider it. Any additional costs or savings to the Crown that may arise from decisions following the review will have a corresponding fiscal impact.

Concessionary Loans (Unchanged)

The Crown has provided loans to local government and iwi-based organisations on a concessionary basis to achieve public policy purposes. Because of their concessionary nature, these loans are written down on draw down to reflect existing market conditions. There is a risk that future market conditions may require a different adjustment. The current carrying value of these loans on the Crown's balance sheet is $605 million.

Defence Force – Operating and Capital Costs (Unchanged)

In 2013, the Government reconsidered New Zealand Defence Force (NZDF) funding, output requirements and capability intentions, through the Defence Mid-Point Rebalancing Review. The review has resulted in increased funding for NZDF in Budget 2014 and Budget 2015. Further operating and capital decisions may be required to achieve Defence White Paper (2010) policy and enable NZDF to manage additional cost pressures over the forecast period.

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.

Health – Health Benefits Limited (Unchanged)

Health Benefits Ltd (HBL) was established in July 2010 to deliver back-office cost savings, helping district health boards (DHBs) to live within their means in the face of increasing costs and tightening budget constraints. In November 2014 the Minister of Health announced that the implementation of HBL's business cases should be transferred to a DHB-owned vehicle by July 2015 following a due diligence process. HBL has a significant and complex change management programme currently underway with DHBs. This requires that four major national business case initiatives are progressed simultaneously by HBL and DHBs, which will be a significant challenge, particularly during this transition period. Until the business cases have been completed and implemented, there is a risk that the anticipated savings may not be achieved.

Internal Affairs – All-of-Government Common Capabilities Sustainable Funding (Unchanged)

A central component of the Department of Internal Affairs' responsibilities as functional lead for All-of-Government ICT and the ICT Strategy and Action Plan is the development and delivery of All-of-Government common capabilities. The Government has agreed that departments and some Crown Entities should migrate to common ICT capabilities, including RealMe. Many of these common capabilities have been developed and are being used and some are still in development. To the extent that these costs cannot be met within agencies' baselines, they may require new funding.

Labour Market – ACC: Work-related Gradual Process Disease and Infection (Changed)

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. An initial adjustment to the liability and an expense of about $1.0 billion to $1.5 billion would need to be reported if such an amendment were to be enacted.

Revenue – Transformation and Technology Renewal (Unchanged)

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

Social Development – Child, Youth and Family Modernisation (Changed)

An external panel is overseeing the development of a new operating model for Child, Youth and Family that sets outs the structure, systems and resources needed to help improve the outcomes for children and young people by strengthening and enhancing the way it operates. While funding for 2015/16 has been included in the fiscal forecasts, the future costs of the proposal are still being developed. To the extent that these cannot be funded from reprioritisation, additional funding from the operating allowance may be required.

Social Development – Welfare Reform Costs (Unchanged)

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 in order to achieve Better Public Services Result One 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 Existing Crown Balance Sheet, Including the FIF, or the Budget Capital Allowance)

Agency Capital Intentions (Unchanged)

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 agency 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.

Arts, Culture and Heritage – Review of Military History Museum Arrangements (Unchanged)

In June 2014, the Government agreed to review the current arrangements around the recording, collecting and exhibiting of New Zealand's military history with a focus on the national level. At this stage it is unclear what the outcome of this business case will be, but this could result in further provision of military history exhibitions. This could require substantial Crown investment.

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 stock take of Crown-owned earthquake-prone buildings. The likelihood, timing and fiscal impact of any earthquake strengthening are uncertain.

Finance – Asian Infrastructure Investment Bank (New)

New Zealand has attended negotiations among prospective members to establish a proposed Asian Infrastructure Investment Bank. This is likely to take the form of a multilateral bank focused on supporting the development of infrastructure in the Asian region, leveraging both public and private funding. The size of any New Zealand contribution depends on membership and rules on the capital shares. The level of capital subscription is currently estimated at between $100 and $150 million, payable across 2016/17 to 2020/21.

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. Should a decision be taken to refurbish the property, a rough-order cost estimate for this upgrade is $100 million over the forecast period.

Lands – Upgrading Landonline (New)

Land Information New Zealand (LINZ) is currently exploring options around the upgrade of Landonline to replace its outdated technology platform and to meet the changing business and technology needs of users. LINZ completed an indicative business case, which received Cabinet approval to go to the detailed business case stage in November 2013. LINZ has now completed a detailed business case which it will submit to Cabinet for approval in 2015. There is insufficient accumulated depreciation to cover the replacement and enhancement cost.

Parliamentary Service – Parliamentary Accommodation (Unchanged)

With the expiry of the lease on Bowen House in December 2018, the Parliamentary Service is identifying and assessing options for future office accommodation which may require capital expenditure with estimates ranging from $40 million to $130 million.

Primary Industries and Food Safety – Investment in Water Infrastructure (Unchanged)

In addition to $120 million already appropriated, the Government will consider providing further capital of up to $280 million in future Budgets to Crown Irrigation Investment Limited as schemes reach the “investment-ready” stage. The Government has made a public statement that it will invest up to $400 million in equity of irrigation schemes.

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. The NZ Transport Agency has advised that it can fund the Auckland Manukau Eastern Transport Initiatives without further Crown funding. Decisions on further Crown financial assistance for the East-West Link and other projects will be made as part of future Budgets.

Transport – Regional State Highways (Unchanged)

A regional state highway acceleration package of $212 million was announced by the Government in June 2014. $115 million of this is subject to the outcome of further investigations. Further funding decisions will be considered as part of Budget 2016.

Transport – Support for KiwiRail (Changed)

The Government in Budgets 2010 to 2015 supported KiwiRail Holdings Limited (KiwiRail) with around $1.5 billion invested in the New Zealand freight rail system. Further funding will be sought by KiwiRail in future Budgets.

Matters Dependent on External Factors

Building and Housing – Divestment and Development of Housing (Changed)

The forecasts reflect divestments and redevelopments of some housing property as part of HNZC's business as usual asset management strategy and other developments in which the Crown has an interest. 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 about the proposed funding of developments, including of Crown-owned land.

Business, Science and Innovation – Crown Revenue from Petroleum Royalties (Unchanged)

The Crown Revenue from Petroleum Royalties is 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 the Crown revenue. The overall impact for the Crown could be negative or positive. International oil prices have fallen by up to 50% over the last 6 months of the current financial year and it is expected that this will lead to a decline in Royalties payable to the Crown of up to $70 million in 2014/15.

Business, Science and Innovation – Impairment in Value of Broadband Investment (Unchanged)

The Government has set aside approximately $1.6 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 somewhat 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.

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 or potential revenues or recoveries 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. The fiscal impact of this is not yet certain.

Caregiver Employment Conditions (Unchanged)

Several cases and funding claims in the disability support and aged care sectors 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 may involve significant costs to the Crown. 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 contracts in circumstances within the ambit of the Courts' decisions.

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. 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 an 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.

Finance – EQC (Unchanged)

EQC is forecasting a cash deficiency in the National Disaster Fund (NDF) arising in the 2015/16 financial year. Under section 16 of the Earthquake Commission Act 1993 the Crown shall provide funding to meet a deficiency in the NDF. Such funding will impact on net debt but not the operating balance or OBEGAL. The financial position of EQC and the amount of any Crown funding carry a high level of uncertainty owing to the nature of EQC's claims liability. An actuarial estimate of the net claims liability and its rate of settlement is included in the forecasts; however, the estimates are sensitive to underlying assumptions such as damage estimates, legal challenges, reinsurance recoveries and the forecast profile of settlements. The Crown's financial position may be adversely impacted if these assumptions are modified over time. Because the net claims liability is large, small percentage changes in the liability can have a material impact on costs and forecasts.

Finance – Goodwill on Acquisition (Unchanged)

As at 30 June 2014, the Government had goodwill on acquisition of a number of sub-entities totalling $628 million. Under New Zealand accounting standards (PBE IPSAS 26), 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 (Unchanged)

International coal prices have deteriorated significantly since Solid Energy's financial restructure in 2013. In September 2014 the Government provided an indemnity for the company's costs of environmental remediation obligations that allowed it to continue operating. The company continues to implement a business strategy to adapt to market conditions; however, there are large challenges ahead. In particular, the international coal price remains depressed and the company has a large tranche of debt maturing in 2016. Any changes to the support arrangements in place, or any 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. 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 which is sensitive to its underlying assumptions such as damage estimates, legal challenges, reinsurance recoveries and the forecast profile of claims settlement. The Crown's financial position may be adversely impacted as these assumptions are modified over time. Because the net claims liability is large, small percentage changes in the liability can have a material impact on costs and forecasts.

Labour Market – 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.

Labour Market – 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.

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 (Unchanged)

The value of student loans is sensitive to assumptions such as the borrower's future income, and general economic factors such as interest rates, unemployment levels, salary inflation and the CPI. As new lending occurs, an initial write-down to fair value will be made, and an expense will be incurred, reflecting the cost the Crown incurs in making an interest free loan and the risk that borrowers may not repay their loans. However, the assumptions made at the time of lending are volatile and are subject to change.

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 be different 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 $1.0 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'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. 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 2014 *Half Year Update*

The following risks have been removed since the 2014 *Half Year Update:*

Expired risk	Reason
Communications – Ultra-Fast Broadband Expanded Scope	Risk materialised.
Revenue – KiwiSaver One-off Enrolment	The cost is no longer estimated to exceed $100 million over five years, owing to the reduction in the number of potential further enrolees.
Social Development – Vulnerable Children	Risk materialised.
Social Development – Support for Children in Hardship	Risk materialised.

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 and other circumstances known to the Government and subject to specific requirements that may have a material effect on the economic or fiscal outlook.[15]

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 certain situations, 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[16] 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 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.

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

16 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 impact is more than $100 million over five years, and either
- a decision has not yet been taken but it is reasonably possible[17] (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[18] to be approved or occur within the forecasting period.

Additionally, the Minister of Finance may determine, under section 26V of the Public Finance Act 1989, that a matter not 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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[17] 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).

[18] 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.[19]

The contingencies have been stated as at 31 March 2015, being the latest set of reported contingencies.

19 "Remote" is defined as being an item with less than a 10% chance of occurring.

Quantifiable Contingent Liabilities and Contingent Assets

Contingent liabilities		
	Status[20]	**31 March 2015 ($millions)**
Guarantees and indemnities		
New Zealand Export Credit Office guarantees	Unchanged[21]	118
Other guarantees and indemnities	Unchanged	105
		223
Uncalled capital		
Asian Development Bank	Unchanged	2,852
International Monetary Fund – promissory notes	Unchanged	1,107
International Bank for Reconstruction and Development	Unchanged	1,094
International Monetary Fund – arrangements to borrow	Unchanged	1,018
Other uncalled capital	Unchanged	18
		6,089
Legal proceedings and disputes		
Tax disputes	Unchanged	406
Other legal proceedings and disputes	Unchanged	53
		459
Other quantifiable contingent liabilities		
Unclaimed monies	Unchanged	120
Other quantifiable contingent liabilities	Unchanged	256
		376
Total quantifiable contingent liabilities		**7,147**
Contingent assets (all under $100 million)		**156**

20 Status of contingent liabilities or assets when compared to the *Half Year Update* published on 16 December 2014.

21 Included as part of other guarantees and indemnities at the *Half Year Update*, as below the materiality threshold.

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) litigation	Unchanged
Air New Zealand litigation	Unchanged
Kiwibank	Unchanged
Treaty of Waitangi claims	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 liabilities were removed: Ministry of Education litigation, Television New Zealand litigation.

Description of Contingent Liabilities

Quantifiable contingent liabilities over $100 million

Guarantees and Indemnities

Guarantees are legally binding promises made by the Crown to assume responsibility for a debt, or performance of an obligation of another party, should that party default. Guarantees generally relate to the payment of money but may require the performance of services. 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.

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

New Zealand Export Credit Office guarantees

The New Zealand Export Credit Office (NZECO) provides a range of guarantee products to assist New Zealand exporters manage risk and capitalise on trade opportunities around the globe. The obligations to third parties are guaranteed by the Crown and are intended to extend the capacity of facilities in the private sector.

$118 million at 31 March 2015 ($93 million at 30 June 2014)

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 2015 $millions	30 June 2014 $millions
Asian Development Bank	2,852	2,728
International Monetary Fund – promissory notes	1,107	1,013
International Bank for Reconstruction and Development	1,094	968
International Monetary Fund – arrangements to borrow	1,018	937

In addition to the uncalled capital above, the Crown Support Deed agreed with Southern Response Earthquake Services Ltd includes two capital subscriptions:

- a $500 million preference share facility under the Crown's agreement dated 5 April 2012 of which $100 million has already been called and paid, with the other $400 million called but unpaid as at 31 March 2015. The balance is forecast to be paid progressively over the period 2016 to 2017, and

- $500 million of uncalled ordinary shares under an amended Crown Support Deed dated 30 January 2013 by which Southern Response may issue a call notice following the payment or redemption of all preference shares. As at 31 March 2015, no call has been made on this facility, however it is now considered probable that approximately $300 million of this subscription will be called and paid, and therefore has been included in the forecast. The extent to which the subscription is called and paid depends on the ultimate cost of settling earthquake claims, which is subject to significant uncertainty. See further description of the risk on page 77.

Legal proceedings and disputes

Tax disputes

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. This contingent liability represents the maximum liability IRD has in respect of these cases.

$406 million at 31 March 2015 ($591 million at 30 June 2014)

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 IRD. The funds are repaid to the entitled owner on proof of identification.

$120 million at 31 March 2015 ($112 million at 30 June 2014)

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, and

c) Other contingent liabilities.

a) *Indemnities*

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. The impact of any funding under this arrangement is limited to core Crown new debt. See further description of the risk on page 77.
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.
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 Referees	Section 11CE of the District Courts Act 1947 Section 4F of the Justices of the Peace 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.

Party indemnified	Instrument of indemnification	Actions 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.	The indemnity relates to costs incurred in removing the dross and disposing of it at another site in Invercargill if required to do so by an appropriate authority.
New Zealand Local Authorities	Section 9 of the Civil Defence Emergency Management Act 2002 Sections 88-89 of the National Civil Defence Emergency Management Plan Order 2005 Section 26 of the Guide to the National 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 under section 9 of the Act. In addition, Government may provide disaster recovery relief funding to councils to assist individuals and communities with immediate needs; and also will consider applications for "special policy" for recovery measures that will mitigate future risk and where the circumstances are exceptional.
New Zealand Railways Corporation	The Minister of Finance signed the indemnity on 1 September 2004	The directors of New Zealand Railways Corporation 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	Guarantees all loan and swap obligations of the New Zealand Railways Corporation.

Party indemnified	Instrument of indemnification	Actions indemnified
Persons exercising investigating powers	Section 63 of the Corporations (Investigation and Management) Act 1989	Indemnifies the Financial Markets Authority (formerly 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 (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.
	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).

b) Legal claims and proceedings

There are numerous legal actions that 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 have a greater impact than $20 million. 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) litigation

There are several legal actions against ACC in existence, arising in the main from challenges to operational decisions made by ACC. Given the stage of proceedings and uncertainty as to outcomes of the cases, no estimate of the financial effect can be made.

Air New Zealand litigation

Air New Zealand is defending two class actions in the United States. One makes allegations of anti-competitive conduct against many airlines in relation to pricing in the air cargo business. Following settlements, four airlines including Air New Zealand continue to defend the claim. A similar, previously reported class action filed in Australia was discontinued against Air New Zealand in June 2014 resulting in legal costs of over $3 million being recovered.

A second class action in the US, alleges that Air New Zealand together with other airlines acted anti-competitively in respect of fares and surcharges on trans-Pacific routes.

Allegations of anti-competitive conduct in the air cargo business in Hong Kong and Singapore were the subject of proceedings by the Australian Competition and Consumer Commission (ACCC). Following a defended hearing, the Federal Court released its decision in October 2014, finding in favour of Air New Zealand. The ACCC has appealed the decision. The appeal will be defended and cross appeals have been filed on selected aspects of the decision.

Kiwibank

In June 2013, a group called Fair Play on Fees announced plans for a representative action against banks in New Zealand in relation to certain default fees charged to New Zealand customers. In November 2013, the group issued proceedings against Kiwibank. The potential outcome of the proceedings cannot be determined with any certainty at this stage.

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 that 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. Failure to successfully defend such actions may result in a liability for historical Treaty grievances in excess of that currently anticipated.

c) 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.

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 PBE IPSAS 19*: 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.

Treaty of Waitangi claims – Settlement Relativity Payments – see page 78.

Description of Contingent Assets

Quantifiable contingent assets over $100 million

No individual quantifiable contingent assets are greater than $100 million as at 31 March 2015. The majority of quantifiable contingent assets relate to likely cash collectible from tax disputes.