
Specific Fiscal Risks

Introduction

This chapter describes the specific fiscal risks of the Crown, including contingent liabilities. The risks are disclosed as either quantified or unquantified, depending on their characteristics. Only contingent liabilities and other specific fiscal risks involving amounts of \$10 million or more in any one year are separately disclosed. Contingent liabilities below \$10 million are included in the “other quantifiable contingent liabilities” total. Comparatives for 30 June 2003 have been adjusted where appropriate to align with the disclosure of new “material” contingent liabilities. The total amount of contingent liabilities remains unchanged.

Specific Fiscal Risks

Specific fiscal risks (excluding contingent liabilities) are a category of government decisions or circumstances that may have a material impact on the fiscal position. The risks have not been included in the main forecasts because their fiscal impact cannot be reasonably quantified, the likelihood of realisation is uncertain and/or the timing is uncertain. The risks disclosed may not eventuate into Government policy and the final cost or saving may differ from the amount disclosed if the policy is developed.

To ensure a practicable and consistent disclosure approach, risks have been reported that have an expected cost or saving of over \$10 million in any one forecast year and either:

- reflect Government decisions or legislative commitments with uncertain fiscal consequences or timing, or
- are generally being actively considered by the Minister of Finance and responsible Ministers (e.g. they have considered written advice or Cabinet papers), or
- are decisions that have been deferred until a later date.

The risks outlined in this chapter would, if they eventuate, impact on the Government’s forecast new operating and capital spending amounts. If the total of all risks considered exceeds the forecast new operating spending amounts in the forecasts, this would impact on the operating balance.

The forecasts incorporate operating and capital forecast spending amounts to accommodate policy initiatives on which decisions have yet to be made. Some risks outlined in this chapter, if they eventuate, would be covered by these amounts and therefore have no impact on the forecasts. These risks have been disclosed to provide an indication of the pressure the risks place upon the forecast spending amounts.

There are a number of other “pressures” on the fiscal position that have not been included as risks. These “pressures” comprise proposals largely generated within individual departments and not yet considered by the Minister of Finance and responsible Ministers. Such items are also expected to be managed within the forecast spending amounts noted above.

Specific fiscal risks do not include:

- normal forecasting risks, such as uncertainty around welfare benefits, SOE/Crown entity surpluses, the impact of regular revaluations of physical assets, finance costs, or fluctuations in external markets
- possible changes to the interpretation of accounting policies, such as the changes to revenue recognition rules and recognition of liabilities
- discussion documents containing proposals that the Minister of Finance and responsible Ministers will not actively consider until the consultation process has been completed.

The Fiscal Responsibility Act 1994 requires that all specific fiscal risks be disclosed, except where it is determined by the Minister of Finance that disclosing a risk is likely to:

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

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

Time-Limited Funding

Time-limited funding does not meet the definition of a “risk” under the Fiscal Responsibility Act, but is further information that is prepared to increase transparency about initiatives with funding profiles that cease or decrease during the forecast period.

The following tables outline those areas where initiatives have time-limited funding that decreases or ceases at some point, using a \$5 million materiality threshold. They are often related to pilot programmes that may or may not be extended. If operating funding were to be appropriated to maintain funding levels for these nine initiatives (ie extend the initiatives beyond their current scheduled completion dates), the total impact would be up

to \$2 million in 2003/04, \$59 million in 2004/05 and \$86 million from 2005/06, which would impact on the operating balance.

Vote	Description of initiative	Operating impact (\$ million)
Agriculture and Forestry	Sustainable Farming Fund	3 in 2004/05, 13 from 2005/06
Corrections	Auckland Central Remand Prison	2 in 2004/05, 7 from 2005/06
Defence Force	Enduring Freedom deployments	18 in 2004/05, 22 from 2005/06
Defence Force	Iraq Provincial Reconstruction Team deployments	4 in 2004/05, 5 from 2005/06
Education	Microsoft Software Licensing	2 in 2003/04, 5 from 2004/05
Education	Tertiary Education Commission	9 from 2004/05
Internal Affairs	Weathertight Homes Resolution Service	5 in 2004/05, 8 from 2005/06
Māori Affairs	Direct Resourcing of Local-Level Solutions	3 in 2004/05, 7 from 2005/06
Social Development	Community Employment Organisations	10 from 2004/05

Statement of Specific Fiscal Risks

The fiscal risks included in the following tables were finalised as at 8 December 2003.

Quantified Risks³

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

Risks as at 8 December 2003	Operating balance	Gross debt	Net worth	(\$ million)
New risks				
ACC – Public Health Acute	Decrease	Increase	Decrease	-11 operating from 2003/04
ACC – Treatment Costs	Decrease	Increase	Decrease	-30 operating from 2004/05
Child, Youth and Family Services – 2003 Residential Services Strategy	Decrease	Increase	Decrease	-13 operating in 2004/05, rising to -31 from 2008/09; -27 capital in 2006/07 and 2007/08
Corrections – Funding of Staff Pay Settlements	Decrease	Increase	Decrease	-11 operating in 2003/04, -18 in 2004/05, -22 from 2005/06
Customs – Enhanced Border Management	Decrease	Increase	Decrease	-3 operating in 2003/04, -14 from 2004/05; -3 capital in 2003/04, -4 in 2004/05 and 2005/06
Health – Extension of the Health Capital Envelope	Decrease	Increase	Decrease	-140 capital in 2006/07 and -100 in 2007/08
Health – Extension of the Health Funding Path	Decrease	Increase	Decrease	-550 operating in 2006/07
New Zealand Defence Force – Environmental Clean-ups of Defence Bases	Decrease	Increase	Decrease	-10 operating in 2005/06 and -5 in 2006/07
New Zealand Defence Force – NZDF Pay and Allowances	Decrease	Increase	Decrease	-25 operating from 2004/05
New Zealand Defence Force – RNZAF – Personnel Increases	Decrease	Increase	Decrease	-16 operating from 2004/05
New Zealand Defence Force – Stand-alone Security Response Organisation	Decrease	Increase	Decrease	-6 operating in 2004/05, -7 from 2005/06; -21 capital in 2004/05
Revenue – Changes to Paid Parental Leave Scheme	Decrease	Increase	Decrease	-30 from 2004/05

3 In the summary tables listing specific risks:

- negative numbers indicate a deterioration in the Crown's financial position
- "N/A" means no effect
- "Unclear" means insufficient information is available to determine the risk's effect.

In this chapter, "Gross Debt" refers to gross sovereign-issued debt.

Risks as at 8 December 2003	Operating balance	Gross debt	Net worth	(\$ million)
Social Development – Future Directions	Decrease	Increase	Decrease	low hundreds of millions in 2004/05, rising to high hundreds of millions in outyears
Transport – Auckland Transport	Decrease	Increase	Decrease	-900 over ten years
Changed risks				
Corrections – Capital Projects	Decrease	Increase	Decrease	-393 capital over 4 years; -126 operating over 4 years
Health – District Health Board Deficits	Decrease	Increase	Decrease	-79 operating in 2003/04, -46 in 2004/05, -45 in 2005/06
Revenue – Exemption for Overseas Earnings	Decrease	Increase	Decrease	-20 operating from 2004/05
Revenue – Taxation of Offshore Portfolio Investment	Increase	Decrease	Increase	+20 operating from 2004/05
Unchanged risks				
ACC – Medical Misadventure Review	Decrease	Increase	Decrease	-25 operating from 2003/04
Customs – Container Security	Decrease	Increase	Decrease	-20 operating from 2004/05
Education – ECE Strategic Plan	Decrease	Increase	Decrease	-120 operating over 4 years
Education – School Property	Decrease	Increase	Decrease	-75 capital in 2003/04, -115 from 2004/05; -1 operating in 2003/04, -9 in 2004/05, -21 in 2005/06, -30 in 2006/07
Education – United Nations Convention on the Rights of the Child	Decrease	Increase	Decrease	-14 operating from 2003/04
Health – Mental Health Blueprint	Decrease	Increase	Decrease	-25 operating in 2004/05, -50 operating in 2005/06, -75 operating in 2006/07, -100 operating in 2007/08, plus additional -25 each year until Budget 2020
New Zealand Defence Force – Defence Capital Injections	Decrease	Increase	Decrease	-749 capital over 4 to 9 years
Revenue – Tax Simplification for Small and Medium Enterprises	Decrease	Increase	Decrease	-20 operating from 2004/05

Unquantified Risks

The risks outlined in this table would, if they eventuate, impact on the Government's forecast new operating and capital spending amounts.

Risks as at 8 December 2003	Operating balance	Gross debt	Net worth
<i>New risks</i>			
Education – Collective Employment Agreements	Decrease	Increase	Decrease
Education – Student Support	Decrease	Increase	Decrease
Finance – Crown Overseas Properties	Unclear	Unclear	Unclear
Health – Refinancing of District Health Board Private Debt	Decrease	Increase	Decrease
Health – Quality and Safety	Decrease	Increase	Decrease
Justice – Courts Capability	Decrease	Increase	Decrease
Lands and Conservation – Achievement of the Government's Objectives for the South Island High Country	Decrease	Increase	Decrease
New Zealand Defence Force – Relocation of NZDF Headquarters	Decrease	Increase	Decrease
Pay and Employment Equity Taskforce	Decrease	Increase	Decrease
State Owned Enterprise Capital Injections	N/A	Increase	N/A
State Services – Electronic Authentication of Identity	Decrease	Increase	Decrease
<i>Changed risks</i>			
Air New Zealand	Unclear	Unclear	Unclear
<i>Unchanged risks</i>			
Education – Partnerships for Excellence	Potentially increase	Increase	Potentially increase
Education – Wananga Capital Injection	N/A	Increase	N/A
Climate Change and Energy Efficiency – Climate Change	Unclear	Unclear	Unclear
Foreign Affairs and Trade – Official Development Assistance	Decrease	Increase	Decrease
Gas Supply	Decrease	Increase	Decrease
Health – Wage Bargaining	Decrease	Increase	Decrease
Housing – Housing Strategy	Decrease	Increase	Decrease
Housing – State Housing Project at Hobsonville	Decrease	Increase	Decrease
Immigration – Immigration Policy	Unclear	Unclear	Unclear
New Zealand Defence Force – Sale of Skyhawks and Aermacchi Trainers	Increase	Decrease	Increase
Police – Capital Projects	Decrease	Increase	Decrease
Revenue – Fringe Benefit Tax Review	Unclear	Unclear	Unclear
Revenue – Gaming Review	Unclear	Unclear	Unclear

Revenue – Taxation of Savings and Investment Vehicles, Including Superannuation Funds	Unclear	Unclear	Unclear
Social Development – Benefit Payment Systems	Decrease	Increase	Decrease
Tourism – Marketing Opportunities with Team New Zealand	Decrease	Increase	Decrease

Risks Removed Since the 2003 *Budget Update*

Risks	Comment
Agriculture and Forestry – Painted Apple Moth	In the forecasts
Child, Youth and Family – Baseline Review	In the forecasts
Conservation – Recognition of Fencing on the Conservation Estate	In the forecasts
Corrections – Output Price Review	In the forecasts
Education – Capital Injections for Tertiary Education Institutions	Not under active consideration
Education – Collective Employment Agreements (<i>principals</i>)	In the forecasts
Education – Improved Internet Access – Project Probe	In the forecasts
Foreign Affairs and Trade – Ministry of Foreign Affairs and Trade Capability	In the forecasts
Government Response to Growth and Innovation Framework Sector Taskforces	In the forecasts
Police – Wage Bargaining	In the forecasts
Social Development – Response to Joychild Report	In the forecasts

Quantified Fiscal Risks

New risks

ACC – Public Health Acute (new risk)

The Government is currently considering 2003/04 funding to reflect increased demand for ACC-funded services through the hospital system. While costs are still being determined, the Government-funded proportion of this is likely to be up to \$11 million in 2003/04 and outyears, which would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: Department of Labour

ACC – Treatment Costs (new risk)

The Government is considering several options to increase access to ACC treatment providers. The potential cost of these options is up to \$30 million operating from 2004/05, which would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: Department of Labour

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

The Department of Child, Youth and Family Services has undertaken a comprehensive review of existing residential services and practices, including consideration of desired outcomes, a review of international good practice and formal forecasting of demand. From this the department has developed a strategy for future residential services - the 2003 Residential Services Strategy. The 2003 Strategy builds on the considerable investment in facilities made in implementing the 1996 Residential Services Strategy.

The Government has agreed in principle to the 2003 Strategy, subject to fully developed and costed proposals. The maximum operating cost is estimated to be up to \$13 million in 2004/05, increasing each year to \$31 million in 2008/09 and outyears, which would decrease the operating balance. The maximum capital cost is estimated to be up to \$27 million in each of 2006/07 and 2007/08, which would increase gross debt.

The risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

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

Source: Department of Child, Youth and Family Services

Corrections – Funding of Staff Pay Settlements (new risk)

The Department of Corrections has concluded pay negotiations for all major employment groups within the Department. The Government is now considering options to fund these settlements. The estimated operating costs of meeting the settlements are \$11 million in 2003/04 and \$18 million in 2004/05, rising to \$22 million in 2005/06 and outyears, which would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amounts.

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

Source: Department of Corrections

Customs – Enhanced Border Management (new risk)

The Government is considering Customs' responses to heightened security concerns, which include proposals for significant increases in Customs' presence at air and sea ports, including additional launches for harbours, estuaries and navigable waterways. This proposal may require operating funding of up to \$3 million in 2003/04 and \$14 million in outyears, which would decrease the operating balance; and capital injections of \$3 million in 2003/04 and \$4 million in 2004/05 and 2005/06, which would increase gross debt.

This risk, if it eventuates, would impact on the Government's forecast new operating and capital spending amounts.

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

Source: New Zealand Customs Service

Health – Extension of the Capital Envelope (new risk)

The Government is considering an extension of the Health capital envelope to 2007/08 to provide adequate planning horizons for DHB capital projects. The cost of this extension has yet to be fully considered by the Government but is likely to be in the order of \$140 million in 2006/07 and \$100 million in 2007/08, which would increase gross debt.

This risk would, if it eventuates, impact on the Government's forecast new capital spending amount.

Source: Ministry of Health

Health – Extension of the Health Funding Path (new risk)

The Government is considering an extension of the Health Funding Path to 2006/07. The cost of this extension has yet to be fully considered by the Government but is likely to be in the order of \$550 million from 2006/07, which would decrease the operating balance.

This risk, if it eventuates, would impact on the Government's forecast new operating spending amount.

Source: Ministry of Health

New Zealand Defence Force – Environmental Clean-ups of Defence Bases (new risk)

The Government is considering the options for dealing with areas of historic contamination at several New Zealand Defence Force (NZDF) bases, including the seabed adjacent to the Calliope Dock at the Devonport Naval Base. The estimated cost of cleaning up identified areas is \$10 million in 2005/06 and \$5 million in 2006/07, which would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: New Zealand Defence Force

New Zealand Defence Force – NZDF Pay and Allowances (new risk)

The NZDF is in the fourth year of a four-year programme to reinstate market relativity to Defence pay and allowances. The Government is considering its options for funding pay and allowances in the NZDF. The estimated operating cost is up to \$25 million in 2004/05 and outyears, which would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: New Zealand Defence Force

New Zealand Defence Force – RNZAF – Personnel Increases (new risk)

The Government is considering what the appropriate personnel levels are to sustain Royal New Zealand Air Force (RNZAF) capabilities over the coming period and to have them aligned to future force structure, now that the RNZAF intends to consolidate its operational capability at Ohakea by 2008. The potential ongoing operating cost of further personnel is up to \$16 million in 2004/05 and outyears, which would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amounts.

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

Source: New Zealand Defence Force

New Zealand Defence Force – Stand-Alone Security Response Organisation (new risk)

New Zealand's ability to respond to chemical, biological, radiological and explosive threats has been under review since 2001. The 2002 Budget provided funding for the establishment of a national chemical and biological response capability. The Government is considering proposals for a more comprehensive and responsive approach to deal with these threats. The estimated operating costs of a stand-alone security response organisation are \$6 million in 2004/05 and \$7 million in 2005/06 and outyears, which

would decrease the operating balance, and capital costs of \$21 million in 2004/05 only, which would increase gross debt.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

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

Source: New Zealand Defence Force

Revenue – Changes to Paid Parental Leave Scheme (new risk)

The Government will consider changes to the Paid Parental Leave scheme for introduction, at the earliest, during 2004/05. Depending on the composition of the final package of changes, the proposals may have an operating cost of up to \$30 million per year, which would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: Department of Labour

Social Development – Future Directions (new risk)

The Government is considering various options for social assistance changes, involving potential changes to Family Income Assistance, the Childcare Subsidy, the Accommodation Supplement and Hardship Assistance. A variety of options are being considered, which may be implemented in a phased approach. The final package will be decided as part of the 2004 Budget, taking into account the affordability of any package in the context of the economic and fiscal situation at the time. The potential costs of the options under consideration at present are in the low hundreds of millions in 2004/05 to the high hundreds of millions in outyears.

This risk has been factored into the Government's forecast new operating spending amounts, therefore any decisions taken will not affect the forecast operating balance.

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

Source: Ministry of Social Development

Transport – Auckland Transport (new risk)

The Government has announced its proposed initiatives towards Auckland's transport issues, which involves an integrated solution including funding, governance and regulatory measures.

The proposals include a 5c per litre increase in petrol excise from 1 April 2005 and a potential Crown contribution of \$900 million over ten years from 2005/06 into the National Land Transport Account, which would increase gross debt. The Government expects to make final decisions on the budget and fiscal management implications arising from these proposals in early 2004.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

Source: Ministry of Transport

Changed risks

Corrections – Capital Projects (changed risk)

The Department of Corrections has estimated that up to a total of \$393 million of capital injections and operating funding of \$126 million will be required over the forecasting period for capital projects to meet future prison muster forecasts (\$398 million capital and \$110 million operating in *Budget Update*).

The actual amounts will depend on the specification and timing of the individual projects and the contracted prices. These estimates include consideration of funding for the:

- Spring Hill Corrections Facility
- Otago Men's Corrections Facility
- Mt Eden Prison
- Auckland Women's Corrections Facility.

Capital injections would increase gross debt while operating funding would decrease the operating balance. This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

The Minister of Finance has yet to fully consider the quantum of these risks.

Source: Department of Corrections

Health – District Health Board Deficits (changed risk)

District health board (DHB) current annual plans signal forecast deficits of \$79 million in 2003/04, \$46 million in 2004/05 and \$45 million in 2005/06 (\$120 million in 2003/04 in the *Budget Update*). The Government has not accepted all the individual plans at this time, and is actively discussing with DHBs their plans and performance against them.

The impact on the operating balance, if any, is unclear. Any deficits above that provided for within the Health Funding Path will decrease the operating balance and increase gross debt. This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

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

Source: Ministry of Health

Revenue – Exemption for Overseas Earnings (changed risk)

The Government is considering options to reduce the tax-related costs for businesses of recruiting overseas workers.

The Government has released a discussion document proposing a time-limited exemption from tax on some or all overseas investment income, for people coming to work as employees in New Zealand. However, any proposal is not expected to be implemented before 2004/05.

The impact of this proposal on the operating balance is likely to be a decrease in the order of \$20 million per annum (unquantified in the *Budget Update*), however the final impact remains unclear as it depends on the options chosen. This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: Inland Revenue

Revenue – Taxation of Offshore Portfolio Investment (changed risk)

The Government intends to release an Issues Paper by the end of this year on reforms to the tax rules for offshore portfolio investment in equity. This paper will contain options arising from work on the offshore application of the Risk Free Return Method but is not limited to that approach (this risk referred only to the Risk Free Return Method in the *Budget Update*).

The impact on the operating balance is unclear at this stage and would depend on the options selected. It is expected to range from being broadly operating balance neutral to increasing the operating balance by between \$20 million and \$40 million per year.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: Inland Revenue

Unchanged risks

ACC – Medical Misadventure Review (unchanged risk)

The Medical Misadventure Account is currently funded partly from the Earners' Account and partly by the Crown through the Non-Earners' Account. A review of the Medical Misadventure Account is underway, considering all aspects of the Account. Potential costs resulting from the Review range from zero to \$47 million, some of which will be covered by ACC Earners' Levy payers.

The potential impact on the operating balance ranges from zero to a decrease of \$25 million per annum from 2003/04.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: Accident Compensation Corporation

Customs – Container Security (unchanged risk)

The Government has approved operating and capital funding in 2003/04 to provide real-time risk assurance and, where necessary, X-ray screening of export containers. The Government has yet to determine the appropriate arrangements for meeting operating costs in 2004/05 and outyears, but is considering fees to be imposed on exporters, importers and transport operators.

The ongoing operating cost is expected to be up to \$20 million in 2004/05 and outyears, which would decrease the operating balance depending on the level of cost recovery. Any additional costs would impact on the Government's forecast new operating spending amount.

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

Source: New Zealand Customs Service

Education – ECE Strategic Plan (unchanged risk)

The Early Childhood Education (ECE) Strategic Plan, which sets out a 10-year action plan for the sector, was released in September 2002. This Plan signals major changes to the funding, regulation and ownership of ECE services. The Government is considering a number of issues related to implementation details, flow-on effects of kindergarten teachers' pay parity, and the balance of Government funding and parent fees.

These decisions may require operating funding that is estimated up to \$120 million by 2006/07 and would decrease the operating balance. This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: Ministry of Education

Education – School Property (unchanged risk)

The Government has provided \$38 million in 2003/04 for school accommodation in the 2003 Budget. Additional capital injections for school accommodation are likely to be required in future years to meet roll growth. Capital injections are estimated to be up to \$75 million in 2003/04 and \$115 million in 2004/05 and each subsequent outyear.

In addition to capital injections, consequential operating costs are likely to be incurred. These are estimated at \$1 million in 2003/04, \$8 million in 2004/05, \$21 million in 2005/06 and \$30 million in 2006/07.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

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

Source: Ministry of Education

Education – United Nations Convention on the Rights of the Child (unchanged risk)

The United Nations Convention on the Rights of the Child obliges New Zealand to confer the rights of the Convention on all children. New Zealand has reserved its right to distinguish between persons according to the nature of their authority to be in New Zealand. However, the Government has indicated that it will undertake work to see if this reservation can be removed. This would involve making some changes to eligibility for some health and education services, which may decrease the operating balance by approximately \$14 million per year.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: Ministry of Education

Health – Mental Health Blueprint (unchanged risk)

The Mental Health Blueprint recommends an increasing funding profile for mental health services. This growth in funding has been included in forecasts to 2003/04, which was the furthest it could be extended to at the time the decision was taken. The Government is expected to consider further increases outside the Health Funding Path of \$25 million in 2004/05, \$50 million in 2005/06, \$75 million in 2006/07, and \$100 million in 2007/08 and an additional \$25 million each year until Budget 2020, which would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

Source: Ministry of Health

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

Implementing the Government's decisions on the future force structure of the NZDF will involve a series of capital acquisitions across all three armed services to achieve the required capability upgrades. The Government has agreed to a capital injection of up to \$1 billion between 2001/02 and 2010/11, of which \$251 million has been agreed⁴, with the bulk likely to be required within the next four years to enable these acquisitions to occur.

The actual expenditure profile will depend on the specification and timing of the individual projects, the contracted prices, and the prevailing exchange rate at the time of purchase.

The Minister of Finance is engaged in a process to consider the individual projects of this risk as they occur. Any capital injections would increase gross debt. This risk would, if it eventuates, impact on the Government's forecast new capital spending amount.

Source: New Zealand Defence Force

⁴ The total amount already agreed was listed as \$287 million in the *Budget Update*. That figure included some funding that was not part of the \$1 billion planned injection, so should have read \$251 million. The substance of this risk has not changed since the *Budget Update*.

Revenue – Tax Simplification for Small and Medium Enterprises (unchanged risk)

The Government released a discussion document in September 2003 containing proposals to reduce tax compliance costs for small to medium enterprises. Depending upon the composition of the package of measures decided after consultation on the discussion document, the proposals may have a fiscal cost of between \$20 million and \$40 million per year, commencing at the earliest from 2004/05, which would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

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

Source: Inland Revenue

Unquantified Fiscal Risks

New risks

Education – Collective Employment Agreements (new risk)

The primary and secondary teachers' collective agreements will expire on 30 April 2004. The Government will need to meet any fiscal impact in 2004/05 and beyond due to the renegotiation of these agreements, including any agreed contribution to the teachers' retirement savings scheme, and any adjustments to individual employment agreements. Any increase in funding required will decrease the operating balance.

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

Education – Student Support (new risk)

Following the release of a discussion document in September 2003, the Government is now considering a package of initiatives relating to Student Support.

The impact, if any, of this proposal on the operating balance or debt is unclear as it depends on the options chosen. Any additional operating cost would decrease the operating balance and any capital injections would increase gross debt.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

Finance – Crown Overseas Properties (new risk)

The Government is considering options relating to the continued use of certain Crown overseas properties. The risk is unquantified as disclosure could compromise any negotiations the Crown may enter, but any additional operating funding will decrease the operating balance, while capital funding would increase gross debt. Alternatively, the sale of any properties would decrease gross debt.

The risk would, if it eventuates, impact on the Government's forecast new capital spending amount.

Health – Refinancing of District Health Board Private Debt (new risk)

All DHB debt owed to private lenders is currently being refinanced with debt supplied by the Crown. The Government is considering early refinancing of DHB private sector debt that was originally set to mature outside the current forecasting period. This would increase gross debt within the forecast period, but reduce the need for refinancing beyond the forecasting period.

Health – Quality and Safety (new risk)

The Government is considering options to improve the quality and safety of the services provided in the disability support sector. The risk is unquantified as policy options have yet to be developed and the amount and timing of any change in funding have yet to be determined.

This risk, if not funded from within the Health Funding Path, would impact on the Government's forecast new operating spending amount.

Justice – Courts Capability (new risk)

The Government is considering options to address immediate and significant operating and capital fiscal pressures in the Ministry of Justice's courts business. This risk is unquantified as the amount of any change in departmental funding is unclear, but any increase in funding to meet additional operating and capital costs would decrease the operating balance and increase gross debt.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

Lands and Conservation - Achievement of the Government's Objectives for the South Island High Country (new risk)

In 2003 the Government agreed a set of objectives for the South Island high country. It is now considering options to achieve and fund these objectives, including the Land Tenure Reform process, and is expected to make decisions as part of the 2004 Budget.

The risk is unquantified as disclosure could compromise the Crown in negotiations, but any additional operating funding would decrease the operating balance and additional capital would increase debt.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

New Zealand Defence Force - Relocation of NZDF Headquarters (new risk)

The NZDF current accommodation leases expire between 2004 and 2006, with the primary location at Stout Street needing to be vacated by March 2006. The NZDF is in negotiations with Capital Properties to consolidate all accommodation requirements for the NZDF, Ministry of Defence and NZ Security Intelligence Service. The Government is considering the options for the term of the lease and the rental mechanisms that will apply.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts. The risk is unquantified as disclosure could compromise the Crown in negotiations.

Pay and Employment Equity Taskforce (new risk)

The Government has established a taskforce to look into issues of pay and employment equity in the public service, public health and education sectors. The taskforce is expected to make recommendations for the Government to consider in March 2004. Given the timing of those recommendations, the uncertainty about the shape of any proposals that may flow from those recommendations and the difficulty in gauging whether any initiatives could be funded within baselines, it is not possible to determine the fiscal cost. However, any increased operating funding would decrease the operating balance.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amounts.

State Owned Enterprise Capital Injections (new risk)

The Government is considering providing additional capital injections to SOEs, subject to there being favourable investment proposals available that would warrant an injection of equity. Proposals to provide additional Crown equity will be considered on a case-by-case basis.

This risk is unquantified because the Minister of Finance has yet to fully consider the quantum of any additional equity to be provided to SOEs, and also because disclosure of amounts in relation to any specific proposal from an SOE could compromise the Crown in commercial activities. This risk would, if it eventuates, impact on the Government's forecast new capital spending amounts.

State Services – Electronic Authentication of Identity (new risk)

The Government has provided funding for the State Services Commission to develop a scoping business case for electronic authentication of identity. It is expected to consider this business case in March 2004. Should the Government proceed with the electronic identification of identity then further funding may be required.

The risk is unquantified as disclosure could compromise the Crown in negotiations, but any additional operating funding will decrease the operating balance, while capital funding would increase debt.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

Changed risks*Air New Zealand (changed risk)*

Air New Zealand and Qantas have announced they wish to form a strategic alliance, with Qantas acquiring a minority equity interest in Air New Zealand. Competition authorities (the Commerce Commission in New Zealand and the Australian Competition and Consumer Commission) have rejected the proposed alliance, as the authorities could not be satisfied that the public benefits from the proposed alliance would outweigh the detriment, but the airlines are appealing these decisions in both countries.

Should the appeal succeed, there may be an impact on the Government's share of Air New Zealand's future earnings, which would impact on the operating balance. This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

Unchanged risks*Education – Partnerships for Excellence (unchanged risk)*

The Government has decided to establish an arrangement called "Partnerships for Excellence" whereby the Crown matches private sector investment in the tertiary sector. This risk is unquantified as funds will be considered on an annual basis subject to budgetary pressures. Depending on the nature of the partnership the operating balance may increase but any capital injections will increase gross debt.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amount.

Education – Wananga Capital Injection (unchanged risk)

Ministers are currently negotiating with one wananga (Māori tertiary institution) over settlement of its Waitangi Tribunal claim. The Waitangi Tribunal has recommended that the wananga be compensated for capital expenditure that has been incurred on facilities to date, and be provided with funding to bring its facilities up to a standard comparable with other tertiary institutions and to meet additional capital requirements. Any capital injection will increase gross debt.

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

This risk would, if it eventuates, impact on the Government's forecast new capital spending amount.

Climate Change and Energy Efficiency – Climate Change (unchanged risk)

The Government has ratified the Kyoto Protocol, and has approved a policy package to meet commitments under the Protocol. The package contains the following elements, which will be targeted at different sectors as appropriate and may be funded through cash or emission units:

- Existing policies aimed at greenhouse gas reduction, including the Waste Strategy renewable programme, and the Energy Efficiency and Conservation strategy.
- A carbon charge with negotiated greenhouse agreements for those firms deemed to be “competitiveness at risk”.
- Emissions' reduction projects.
- Methane and nitrous oxide mitigation research.
- Mechanisms to incentivise the establishment and enhancement of carbon sinks.

At this stage, it is unclear what impact the decision to ratify the Protocol will have on the operating balance, either positive or negative, since this is closely related to the detailed design of the policy options.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

Foreign Affairs and Trade – Official Development Assistance (unchanged risk)

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

Gas Supply (unchanged risk)

The Government is considering options to improve certainty of gas supply, including for electricity generation. This involves direct negotiations with industry parties.

This risk is unquantified as disclosure could compromise the Crown in negotiations and commercial activities. This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

Health – Wage Bargaining (unchanged risk)

The New Zealand Nurses' Organisation has indicated it will be seeking substantial pay increases in a series of wage negotiations over the next six to twelve months. The Minister of Health has indicated to DHBs that the outcome of these negotiations must be met within their three-year Health Funding Paths. If this were not the case it would decrease the operating balance.

This risk is unquantified, as disclosure could compromise the Crown in negotiations. This risk, if not funded from within the Health Funding Path, would impact on the Government's forecast new operating spending amount.

Housing – Housing Strategy (unchanged risk)

In December 2002 the Government agreed that the Housing New Zealand Corporation (HNZC) would develop a New Zealand Housing Strategy involving consultation with all key stakeholders in the housing and wider social sectors.

The risk is unquantified as the amount or timing of any change in funding is unclear, but any increase in funding to meet additional operating costs would decrease the operating balance and any new capital contributions would increase gross debt.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

Housing – State Housing Project at Hobsonville (unchanged risk)

The Government has announced that the HNZC will acquire, under the Housing Act 1955, NZDF land at Hobsonville deemed surplus to Defence requirements but suitable for state housing purposes. Land made available for purchase by Defence was acquired by HNZC at the end of 2002/03. Additional land is expected to become available over the next three to four years.

Depending on development options taken and timing, the Corporation may require additional capital from the Crown, which would increase gross debt. This risk would, if it eventuates, impact on the Government's forecast new capital spending amount.

Immigration – Immigration Policy (unchanged risk)

The Government has made some high-level decisions about business immigration policies and is presently considering a number of implementation issues. The impacts on the operating balance and debt are unclear as they depend on the options chosen.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

New Zealand Defence Force – Sale of Skyhawks and Aermacchi Trainers (unchanged risk)

As a result of the Government's decisions on the future force structure of the NZDF, the NZDF is in the process of selling the Skyhawks and Aermacchi trainers. These sale proceeds would increase the operating balance and decrease gross debt.

This risk is unquantified as disclosure could compromise the Crown in the sale process. This risk would, if it eventuates, be considered against the Government's forecast new operating and capital spending amounts.

Police – Capital Projects (unchanged risk)

New Zealand Police has identified a number of Police stations that require capital work to bring them up to a modern operating standard.

The timing, scale and funding for new assets are unclear at this stage, but any capital injections would increase gross debt. This risk would, if it eventuates, impact on the Government's forecast new capital spending amount.

Revenue – Fringe Benefit Tax Review (unchanged risk)

The Government has decided to review the fringe benefit tax regime. The review will focus on reducing the difficulty and cost to employers of complying with fringe benefit tax, while ensuring the revenue base is maintained. A discussion document on this issue was released in December 2003. Any legislative changes resulting from the review will be introduced in 2004.

Any impact on the operating balance from any legislative amendments is unclear at this stage. This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

Revenue – Gaming Review (unchanged risk)

The Gaming Review was completed and the Gambling Act has now been passed. The Government, however, is still considering the taxation of gaming. Any impact on the operating balance arising from a response, whether positive or negative, is unclear.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

Revenue – Taxation of Savings and Investment Vehicles, Including Superannuation Funds (unchanged risk)

The Government is broadly considering whether the tax system creates impediments to adequate saving, whether savings intermediaries are correctly taxed, and whether the current taxation of retirement saving is equitable.

The impact of any proposal on the operating balance would vary widely by the options chosen and the method of implementation. This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

Social Development – Benefit Payment Systems (unchanged risk)

The Ministry of Social Development is considering the future development and/or replacement of its income benefit payment systems (SWIFTT and TRACE). Decisions will be made when an information technology strategy has been developed taking into account the Ministry's *Statement of Intent* and the results of the work on the reform of the social assistance system. Capital injections for development costs will have an impact on debt, and operating funding will affect the operating balance. The quantum of the risk cannot be determined until decisions have been made about which options are to be chosen.

This risk would, if it eventuates, impact on the Government's forecast new operating and capital spending amounts.

Tourism – Marketing Opportunities with Team New Zealand (unchanged risk)

The Government has announced that it has initially committed \$6 million to Team New Zealand to retain team members for the 2007 America's Cup in Spain.

The Government may commit up to a maximum of \$34 million in total as a marketing partner for the challenge. The final level of the Government's contribution will depend on an assessment of the potential economic benefits that can be leveraged off the next regatta in Europe and Team New Zealand's ability to raise substantial funding from the private sector.

This risk would, if it eventuates, impact on the Government's forecast new operating spending amount.

Contingent Liabilities

Contingent liabilities are costs that the Crown will have to face if a particular event occurs. Typically, contingent liabilities consist of guarantees and indemnities, legal disputes and claims, and uncalled capital. The contingent liabilities facing the Crown are a mixture of operating and balance sheet risks, and they can vary greatly in magnitude and likelihood of realisation. In general, if a contingent liability were realised it would reduce the operating balance and net worth, and increase net Crown debt. However, in the case of contingencies for uncalled capital, the negative impact would be restricted to net Crown debt.

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

Contingent liabilities have been stated as at 31 October 2003, being the last set of published contingent liabilities.

Details of each of the following contingent liabilities can be accessed from the Treasury website at www.treasury.govt.nz/forecasts/defu/2003/.

Quantifiable Contingent Liabilities

Guarantees and indemnities	Status⁵	(\$ million)
Cook Islands - Asian Development Bank loans	Unchanged	18
Indemnification of receivers and managers - Terralink Limited	Unchanged	10
Indemnification of touring exhibitions	Changed	164
Mighty River Power Limited – guaranteed payment obligations	Unchanged	50
Ministry of Transport - funding guarantee	Unchanged	10
Post Office Bank - guaranteed deposits	Changed	13
Guarantees and indemnities of state-owned enterprises and Crown entities	Changed	4
Other guarantees and indemnities	Changed	78
		347
Uncalled capital		
Asian Development Bank	Changed	1,159
European Bank for Reconstruction and Development	Unchanged	14
International Bank for Reconstruction and Development	Changed	1,345
		2,518
Legal proceedings and disputes		
Health - legal claims	Unchanged	104
Tax in dispute	Changed	187
Legal claims and disputes of state-owned enterprises and Crown entities	Changed	9
Other legal claims	Changed	81
		381
Other quantifiable contingent liabilities		
International finance organisations	Changed	1,016
Reserve Bank - demonetised currency	Unchanged	23
Social Development - claim for judicial review	Changed	70
Transpower New Zealand Limited	Changed	60
Other quantifiable contingent liabilities of state-owned enterprises and Crown entities	Changed	9
Other quantifiable contingent liabilities	Changed	44
		1,222
		4,468

5 Relative to reporting in the 30 June 2003 Crown financial statements.

Unquantifiable Contingent Liabilities

Institutional guarantees and indemnities	Status
Air New Zealand Limited	Unchanged
Asure New Zealand Limited	Unchanged
At Work Insurance Limited	Unchanged
Auckland rail lease	Unchanged
Crown research institutes	Unchanged
DFC New Zealand Limited (under statutory management)	Unchanged
District Court Judges, Justices of the Peace, Coroners and Disputes Tribunal Referees	Unchanged
District health boards	Unchanged
Earthquake Commission	Unchanged
Electricity Corporation of New Zealand Limited	Unchanged
Fletcher Challenge Limited	Unchanged
Ministry of Fisheries - indemnity provided for delivery of registry services	Unchanged
Housing New Zealand Corporation	Unchanged
Indemnities against acts of war and terrorism	Unchanged
Maui Partners	Unchanged
National Provident Fund	Unchanged
New Zealand Railways Corporation	Changed
Persons exercising investigating powers	Unchanged
Public Trust	Unchanged
Purchasers of Crown operations	Unchanged
Reserve Bank of New Zealand	Unchanged
State Insurance Office tax liabilities	Unchanged
Works Civil Construction	Unchanged
Works Consultancy Services	Unchanged
Other unquantifiable contingent liabilities	
Environmental liabilities	Unchanged
Genesis Power Limited	Unchanged
New Zealand Post Primary Teachers' Association	Unchanged
Sale of Crown assets	Unchanged
Treaty of Waitangi claims	Unchanged
Treaty of Waitangi claims - settlement relativity payments	Unchanged