STATEMENT 9: RISKS TO THE BUDGET

Contents

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Part I: Statement of risks

INTRODUCTION

The forward estimates of revenue and expenses in the 2002-03 Budget incorporate assumptions and judgements based on information available at the time of publication. A range of factors may influence the actual budget outcome in future years. The *Charter of Budget Honesty Act 1998* requires these factors be disclosed in a Statement of Risks in each Economic and Fiscal Outlook Report. The purpose of this disclosure is to increase the transparency of the fiscal projections and ensure that they remain 'on-balance' estimates.

Events that could affect fiscal outcomes include:

- changes in economic and other parameters;
- matters which have not been included in the fiscal forecasts because of uncertainty about their timing, magnitude and/or likelihood; and
- the realisation of contingent liabilities.

ECONOMIC AND OTHER PARAMETERS

Some degree of uncertainty is attached to the budget and forward estimates for both revenues and expenses.

The major factors influencing expected revenues and expenses in any year are typically changes in forecasts of economic and non-economic parameters. Over the long-term, differences between the economic parameter forecasts and outcomes have not caused any clear bias toward understatement or overstatement of expenses and revenue — and therefore the budget balance. The sensitivity of the estimates to major economic parameters is discussed in Part II of this Statement.

Fiscal risks

Fiscal risks are general developments or specific events that may have an effect on the fiscal outlook. In some cases, the events simply raise the possibility of some fiscal impact. In other cases, some fiscal impact may be reasonably certain, but it will not be included in the forward estimates because the timing or magnitude is not known. Fiscal risks may affect expenses and/or revenue and may be positive or negative on expenses, revenue and/or the budget balance.

Specific sources of fiscal risk include:

- litigation currently before the courts; and
- possible Senate rejection or amendment of budget measures or other legislation before the Parliament.

Some fiscal risks are reflected in the Contingency Reserve and are therefore included in the aggregate expenses and budget balance estimates and not the Statement of Risks.

Contingent liabilities

Contingent liabilities are defined as costs the Government will have to face if a particular event occurs. They include loan guarantees, non-loan guarantees, warranties, indemnities, uncalled capital and letters of comfort. These costs are in addition to those recognised as liabilities in the consolidated financial statements of the General Government Sector of the Commonwealth.

Contingent liabilities differ from fiscal risks in that they are generally more readily quantifiable and clearly defined.

The Commonwealth's major exposure to contingent liabilities arises out of legislation providing guarantees over certain liabilities of Commonwealth controlled financial institutions (that is, the Reserve Bank of Australia and the Export Finance and Insurance Corporation) and the now fully privatised Commonwealth Bank of Australia.

The strategies for managing these exposures are aimed (as far as possible) at ensuring the underlying strength and viability of the entities involved, so that the guarantees are not triggered. Similar strategies may be adopted in relation to entities not subject to explicit guarantees.

Other arrangements are in place to govern the entering into, and monitoring of, contingent liabilities, such as indemnities and uncalled capital. Uncalled capital is primarily associated with international financial institutions such as the International Bank for Reconstruction and Development, the Asian Development Bank and the European Bank for Reconstruction and Development. Arrangements for capital contributions to these institutions, including contingent liabilities, are approved by Parliament and reports on the institutions are provided annually by the Government to Parliament.

Consistent with Australian Bureau of Statistics (ABS) standards, transactions concerned with the management of international reserves and the monetary system are classified as financing transactions and do not impact on the fiscal or operating balance. Contingent liabilities (and assets) with the International Monetary Fund (IMF) are accordingly not shown below.

Details of fiscal risks and contingent liabilities

Fiscal risks and contingent liabilities with a possible impact on the forward estimates greater than $20 million in any one year, or $40 million over the forward estimates period, are listed below. Information on fiscal risks takes account of decisions of Parliament and other developments up to the close of parliamentary business on 30 April 2002. In general, information on contingent liabilities is based on information provided by departments and agencies and is current to 31 March 2002 (or a later date as indicated where that information is available). However, in some cases, earlier dates are used and noted in the relevant section.

Information on contingent liabilities is also provided in the annual financial statements of departments and non-budget entities.

FISCAL RISKS — REVENUE

Revenue forecasts, like all forecasts, are subject to a margin of error.

An implication of the degree of uncertainty surrounding the revenue forecasts is that, while many of the forecasts are reported to the nearest million dollars for budget accounting purposes, they should not be interpreted as implying an equivalent level of forecast precision.

The various risks influencing the accuracy of the revenue forecasts are outlined below.

General risks

The forward estimates of revenue are subject to a number of general pressures that can adversely affect revenue collections. These general pressures include: tax avoidance; developments in communications technology and workplace arrangements; and court decisions. These pressures may result in a shift in the composition of revenue collected from the various tax bases and/or a change in the size of the tax base. The revenue forecasts include an appropriate allowance for these factors, given the data available.

Specific risks

The Government has announced a number of measures to date that have already been factored into the forward estimates of revenue but are yet to be passed by Parliament. Should the passage of legislation relating to these measures be delayed, amended or rejected, the forward estimates would need to be adjusted.

Renegotiation of the double tax agreement (DTA) with the United Kingdom

Australia has commenced negotiations with the United Kingdom to revise the current DTA, which has been in effect since 1967. The aim of the negotiations is to modernise the DTA to take account of changes in the tax systems and tax policies of each country. Depending on the negotiated outcome, changes to the DTA could have positive as well as negative revenue effects and implications for DTAs Australia has with other countries.

Timor Sea Treaty

Australia is currently in negotiations with the United Nations Transitional Administration in East Timor (UNTAET) and East Timor on the Timor Sea Treaty which will provide a legal framework for the exploration and exploitation of petroleum resources in the Timor Sea. The outcome of negotiations will be subject to ratification by both the Australian and East Timorese Parliaments. The outcome of this process could have implications for Australia's revenue from oil and gas developments in the Timor Sea.

FISCAL RISKS — EXPENSES

Agriculture, Fisheries and Forestry

Compensation claim for defective administration

The Department of Agriculture, Fisheries and Forestry is considering a claim made under 'The Scheme for Compensation for Detriment Caused by Defective Administration' (CDDA). CDDA is an administrative scheme established in 1995 to enable Commonwealth agencies to compensate persons who have been adversely affected by the defective action or inaction of agencies but who have no other avenues to seek redress. The claim, for an amount of $68.1 million, relates to a decision in 1985-86 by the then Export Inspection Service to ban the export of sultana table grapes.

Defence

Litigation cases

The Department of Defence is involved in a wide range of litigation and other claims for compensation and/or damages that may result in litigation where the matters have yet to be finalised by negotiation or, where required, litigation. Various claims, the subject of cases that have yet to be heard or are part heard, await a decision on what (if any) damages and/or costs should be paid to the claimant. The litigated and non-litigated claims include common law liability claims and claims before the Human Rights and Equal Opportunity Commission. The litigation also includes asbestos claims. In total there are about 350 claims, with a value of approximately $90 million.

Finance and Administration

Member choice and Commonwealth superannuation arrangements

The Government's policy for new superannuation arrangements for Commonwealth employees has been provided for in the forward estimates. These new arrangements provide for the closure of the Public Sector Superannuation Scheme (PSS) to new employees and would allow new employees to join a complying superannuation fund or retirement savings account (RSA) offered by their employer. The arrangements also provide for existing Commonwealth Superannuation Scheme (CSS) and PSS members to choose to join another fund or RSA. Subject to introduction of new legislation into Parliament to give effect to this policy, the estimates are based on an assumed start date of 1 July 2003. A later start date would improve the underlying cash balance from 2003-04.

Department of Finance and Administration litigation

The Department of Finance and Administration is involved in litigation where a counter-claim for damages has been lodged against the Commonwealth. The counter-claim claims damages of $4.3 billion against the Commonwealth although the basis for this amount is yet to be fully provided.

Asset sales — Telstra

The forward estimates include the effect of the sale of the Commonwealth's shareholding in Telstra, noting that the level of proceeds will depend, inter alia, on the prevailing levels of world equity markets at the time of the sale. The sale of the Commonwealth's remaining shareholding in Telstra is dependent on the passage of legislation through the Parliament. The Government has committed not to introduce such legislation until it is satisfied arrangements exist to deliver adequate services, in particular to rural and regional Australia.

Asset sales — Sydney Airports Corporation Limited

The budget estimates include the effect of the sale of Sydney Airports Corporation Limited. The Government announced on 24 September 2001 that the sale would be delayed until early 2002. The sale was originally announced in the 2001-02 Budget and was expected to be completed in the latter part of 2001. On 11 March 2002, the Government announced the recommencement of the sale process, with the sale timetable to be determined having regard to the Government's commitment to securing the best possible outcome for Australian taxpayers. The level of proceeds to the Commonwealth will depend on market forces at the time of the sale.

Health and Ageing

Major new listings — Pharmaceutical Benefits Scheme and Medicare Benefits Scheme

From time to time items are added to or removed from the Medicare Benefits Scheme and Pharmaceutical Benefits Scheme schedules following independent assessments of cost-effectiveness. Major new developments in medicines or medical procedures could result in increases in expenses that exceed the provision in the forward estimates. Similarly, significant shifts in usage patterns, which may occur for particular drugs or groups of drugs from time to time, could result in increases in expenses that exceed the provision in the forward estimates. It is not possible to quantify the fiscal risk arising from such potential developments.

Immunisation funding mechanism

Future vaccine technology will result in new vaccines substituting for those already in use (for example, multivalent vaccines which combine several vaccines into one) and, as a consequence, could result in higher unit costs of vaccine within the routine schedule. Given the nature of current vaccine technology and the possible introduction of new vaccines, specific costs cannot be precisely quantified at this stage.

Immigration and Multicultural and Indigenous Affairs

Unauthorised boat arrivals and processing of asylum seekers

The number of unauthorised boat arrivals and asylum seekers is difficult to predict. In response to a surge in unauthorised boat arrivals in 2001, the Government adopted additional measures to counter this problem. As at April 2002, no unauthorised boat arrivals had reached mainland Australia since the new measures were introduced. The 2002-03 and forward estimate years provide for an estimated 4,500 unauthorised boat arrivals in each year. If the reduction in arrival numbers since late 2001 is sustained, the funding requirements could be considerably lower.

The International Organisation for Migration and the United Nations High Commissioner for Refugees are coordinating the processing of asylum seekers in third countries. The Australian Government has given an undertaking to fully fund processing costs of these organisations. The costs will be dependent upon processing numbers and times, approval rates and the level of security required to manage the processing centres.

Industry, Tourism and Resources

Corporatisation of the Snowy Mountains Hydro-electric Scheme — environmental flows into the Snowy and Murray Rivers

The Commonwealth is providing $75 million over 10 years until 2012-13 as its contribution to water savings projects as part of a commitment with the New South Wales and Victorian governments to increasing environmental water flows in the Snowy and Murray Rivers. The establishment of a joint government entity to oversee the investment in the water savings projects will occur after the Scheme is corporatised and the responsibility for the Scheme's operation and assets has been transferred to Snowy Hydro Limited. The timing of the expenditure on water savings projects will be driven by the corporatisation process and on how quickly a programme of works can be developed and implemented by the joint government entity. There may be a need to bring forward Commonwealth expenditure.

It is expected that the Commonwealth will contribute, in accordance with its 13 per cent shareholding in Snowy Hydro Limited, to an indemnity from the governments to the company for liabilities arising in relation to the release of Snowy River increased flows.

Corporatisation of the Snowy Mountains Hydro-electric Scheme — repayment of debt to the Commonwealth

Corporatisation of the Scheme in 2001-02 will involve the refinancing and repayment of debt to the Commonwealth in 2002-03. The intention is for the refinancing to be completed within six months of corporatisation. The market value of the debt to be repaid is expected to be in the order of $887 million. Detailed arrangements are being finalised between the Commonwealth, New South Wales and Victorian Governments, as shareholders in Snowy Hydro Limited, and the company that will own and manage the Scheme following corporatisation. It is expected that the refinancing of the debt will require some capital contribution from shareholders.

Australian Magnesium Corporation (AMC)

The Commonwealth has conditionally agreed to offer a guarantee to cover borrowing by AMC to assist in developing a magnesium smelting facility in Stanwell which will commercialise Australian-developed magnesium refining technology. The maximum value of the guarantee is $100 million. The loan itself is to be provided by a lender suitable to the Commonwealth.

Treasury

International Monetary Fund (IMF) assistance to Thailand

Australia's offer to provide bilateral financing of up to $1 billion in support of the IMF programme in Thailand was taken up in the form of a series of currency swaps between the Reserve Bank of Australia (RBA) and the Bank of Thailand. Under the swap arrangements, the RBA provided $US862 million to the Bank of Thailand in exchange for Thai baht. From March 2001, the Bank of Thailand began repaying the swaps as scheduled. Currently, $US402.5 million of the facility remains outstanding. Repayment in full is scheduled to occur no later than July 2004. Changes to the schedule of repayments outstanding may result in the RBA dividend stream in the forward estimates being affected.

Transitional arrangements for reforms to Commonwealth-State financial relations

The Commonwealth has guaranteed that in each of the transitional years following the introduction of *The New Tax System*, each State's budgetary position will be no worse off than had reforms to Commonwealth-State financial relations not been implemented. The amount of funding each State would have had available to it under the previous system of financial relations is known as the Guaranteed Minimum Amount (GMA).

To meet this commitment, the Commonwealth has implemented arrangements for the transitional years. The Commonwealth will pay Budget Balancing Assistance equivalent to any shortfall of GST below a State's GMA. As a result of these arrangements, changes in the components of the GMA or a shortfall in estimated GST revenue over the forward estimates period might result in increased expenses to the Commonwealth.

United Medical Protection (UMP)/Australasian Medical Insurance Ltd (AMIL) Guarantee

The Government has written to medical practitioners insured by UMP / AMIL stating that the Commonwealth will guarantee to the provisional liquidator, or to any other subsequently appointed liquidator, the obligations of UMP / AMIL to pay any amount properly payable in the period 29 April to 30 June 2002 in respect of claims under a current or past policy. The Commonwealth has stated that it will provide a guarantee to the provisional liquidator, or to any subsequently appointed liquidator, to enable the provision of cover in respect of valid claims that arise at any time for: holders of a current policy, for events that occur between 29 April and 30 June 2002; and holders of a current policy that expires and is renewed by the provisional liquidator between 29 April and 30 June 2002, for insured events that occur before 30 June 2002. These proposed guarantees will apply to the extent that the provisional liquidator is unable to meet UMP / AMIL's obligations under these policies from UMP / AMIL's assets. The liabilities cannot be quantified, as a reliable estimate cannot be produced at this time.

CONTINGENT LIABILITIES — QUANTIFIABLE

Attorney-General's

Indemnities relating to the Air Security Officer programme

The Commonwealth has entered into indemnity agreements with Australian airlines that agree to fly aircraft with Air Security Officers on board. The indemnity agreements limit the Commonwealth's exposure up to a maximum of $2 billion per incident. The indemnity applies to the extent that any loss is not covered by existing relevant insurance policies held by the airline and only applies where the airline(s) can prove that an action on the part of an Air Security Officer under or in connection with the Air Security Officer Programme caused a loss.

Communications, Information Technology and the Arts

Art Indemnity Australia

The Government indemnifies cultural objects loaned to exhibitions held in museums and galleries. The estimated indemnified amount of exhibitions in 2002-03 is $1.185 billion. However, the exact amounts involved would vary with the exchange rate applying at the time any claim for loss or damage to an artwork or heritage object loaned from overseas is paid and the extent of the loss/damage. Most of the Commonwealth risk in indemnifying exhibitions is insured through Comcover. Exceptions include uninsurable risks such as acts of war and terrorism, which continue to be borne solely by the Commonwealth.

Defence

Military compensation

A contingent liability of an estimated $25 million exists in relation to military compensation claims. This amount relates to outstanding claims for non-economic loss as a consequence of the Federal Court decision in *Schlenert v the Australian and Overseas Telephone Corporation 1995*.

ADI Limited — warranty on sale

On completion of the sale of ADI Limited on 29 November 1999, the Commonwealth provided warranties relating to the accuracy of representations to the purchaser regarding a number of matters. Breaches of Commonwealth warranties are subject to a limit of liability of $25 million for warranty claims arising from the Sale Agreement, except in relation to breaches of warranty relating solely to Commonwealth contracts or claims where the limit is $50 million. In November 2000, the purchaser, Transfield Thomson CSF Investments Pty Ltd, lodged 11 claims against the Commonwealth on the grounds of breach of warranty on sale, common law damages and damages under the *Trade Practices Act 1974*. The total value of the claims is between $5 million and $12 million.

Education, Science and Training

Commonwealth loan guarantees — Group Training

The Minister for Education, Science and Training has authorised Commonwealth guarantees on a limited number of loans made to Commonwealth-endorsed Group Training companies. These loans provide access to additional working capital required to expand the number of apprentices and trainees that may be employed through Group Training companies. The maximum guarantee of each loan is $175,000 with the total value of all guarantees capped at $30 million. As of 31 March 2002, the Commonwealth has issued three loan guarantees for $175,000 each.

Finance and Administration

ComLand Limited

The Commonwealth explicitly guarantees bank borrowings by ComLand Limited up to a limit of $60 million, comprising $50 million for principal and $10 million for accrued interest and other costs.

Australian Industry Development Corporation (AIDC)

As at 31 March 2002, the AIDC's contingent liabilities were approximately $127 million in respect of guarantees and credit risk facilities. The AIDC's other guaranteed borrowings totalled approximately $1.34 billion as at 31 March 2002. These have been fully offset by holdings in Commonwealth Government securities and certain hedging instruments, all of which are fully guaranteed by Warburg Dillon Read (formerly known as UBS Australia Ltd).

Foreign Affairs and Trade

Export Finance and Insurance Corporation (EFIC)

The Commonwealth guarantees the due payments by EFIC of money that is, or may at any time become, payable by EFIC to any body other than the Commonwealth. As at 31 March 2002, the Commonwealth's total contingent liability was $7.3 billion, comprising EFIC's balance sheet liabilities ($0.9 billion), contracts of insurance and guarantees, overseas investment insurance and political risk insurance ($3.6 billion) and national interest account liabilities ($2.8 billion).

Industry, Tourism and Resources

Liability for damages caused by space activities

The Commonwealth Government requires anyone seeking approvals under the *Space Activities Act 1998* to insure up to the level of Maximum Probable Loss (MPL), up to a maximum of $750 million per launch or return of a space object. The Commonwealth also accepts all liability for damage suffered by Australian nationals up to a value of $3 billion above MPL.

Snowy Mountains Hydro-electric Authority (SMHEA)

The *Snowy Mountains Hydro-electric Power Act 1949* provides that the Commonwealth may guarantee borrowings by SMHEA. The Authority has issued inscribed stock to finance capital works of the Scheme. The borrowings are subject to explicit Commonwealth guarantees. As at 31 March 2002, the face value of guaranteed borrowings was $181 million, having a net value of $136 million after adjustment for the unamortised discount.

Corporatisation of SMHEA will result in the inscribed stock being assumed by the Commonwealth in accordance with the *Snowy Hydro Corporatisation Act 1997*.

Transport and Regional Services

Maritime industry reform

On 18 August 1998, the Commonwealth provided a guarantee to cover borrowings made by the Maritime Industry Finance Company (MIFCo) to finance redundancy-related payments in the stevedoring and maritime industries. Outstanding borrowings covered by the guarantee as at 31 March 2002 were $141 million.

Aviation War Risk Insurance — indemnities for Australian carriers, airports and service providers

Following terrorist attacks in the United States on 11 September 2001, regular insurance cover for claims arising out of war and terrorism was withdrawn or significantly limited, placing global aviation operations at risk. The Commonwealth agreed to provide third party war indemnity cover up to US$5 billion per aircraft per event, to air carriers for one month with monthly extensions if required.

On 28 September 2001, the Government announced the extension of the third party war risk indemnity to all key service providers and facilities associated with the Australian aviation sector. The cover for all affected parties is the gap between commercially available war risk cover and the cover the party had under its policy prior to the terrorist attacks.

As at 29 April 2002, indemnities have been provided to 20 parties: 8 carriers (6 airlines and 2 cargo carriers), 6 airports and 6 other service providers.

The notional upper limit of the Government's contingent liability for these indemnities is approximately A$21.28 billion, based on the difference between the amount of insurance available commercially and the entity's previous level of cover. The individual contingent liabilities range from A$50 million to A$2.7 billion. It is extremely unlikely that the total liability would be called upon as facilities are spread across Australia, nonetheless, a terrorist incident could involve claims from several indemnified parties.

As from July 2002, the Government will provide the indemnity on a rolling three-monthly basis and charge a fee. Eligible operators will continue to obtain and maintain commercial insurance cover for terrorism and war to the fullest extent available in the market.

Treasury

Guarantees under the Commonwealth Bank Sale Act 1995

Under the terms of the *Commonwealth Bank Sale Act 1995*, the Commonwealth has guaranteed various liabilities of the Commonwealth Bank of Australia (CBA), the Commonwealth Bank Officers' Superannuation Corporation (CBOSC) and the Commonwealth Development Bank.

The guarantee for the CBA relates to both on and off-balance sheet liabilities. Of the existing contingent liability, 36 per cent involves off-balance sheet liabilities. As at 30 June 2001 (the latest available figures), the balance of the guarantee was $13.7 billion, a reduction of $5.6 billion on the previous year.

The guarantee for CBOSC covers the due payments of any amount that is payable to or from the Fund, by CBOSC or by the Bank, in respect of a person who was a member, retired member or beneficiary of the Fund immediately before 19 July 1996. Total accrued benefits at 30 June 2001 have been valued at $3.9 billion. The outstanding value subject to the guarantee is estimated to be $3.7 billion.

As of 1 July 1996, the Commonwealth Development Bank ceased to write new business and no additional liabilities are being incurred. The existing contingent liability will gradually decline with the retirement of existing loans and exposures. The revised estimate for the balance of this guarantee was $18 million as at 30 June 2001.

Reserve Bank of Australia (RBA) guarantee

This contingent liability relates to the Commonwealth's guarantee of the liabilities of the RBA. The major component of RBA liabilities relates to Notes (that is, currency) on Issue. This treatment of Notes largely relates to the historical convention of the convertibility of Notes to gold — coins are not treated as a liability in the

Commonwealth's accounts. As at 31 December 2001, Notes on Issue totalled $34.1 billion. In total, the guarantee for the RBA was $50.3 billion as at 31 December 2001.

Uncalled capital subscriptions — international financial institutions

The liability relates to the value of the uncalled portion of the Commonwealth's shares at 30 March 2002 in the International Bank for Reconstruction and Development (US$2.8 billion — estimated value A$5.2 billion), the Asian Development Bank (US$2.4 billion — estimated value A$4.6 billion), the European Bank for Reconstruction and Development (US$81.7 million plus EUR77.5 million — estimated value A$281 million), and the Multilateral Investment Guarantee Agency (US$26.5 million — estimated value A$49.8 million).

CONTINGENT LIABILITIES — UNQUANTIFIABLE

Attorney-General's

Native title costs

The Commonwealth has offered to assist the States and Territories in meeting compensation costs associated with native title. The amounts that might be paid by the Commonwealth will be subject to the terms of financial assistance agreements being negotiated with the States and Territories and liabilities arising from the 1998 amendments to the *Native Title Act 1993*. The Commonwealth's liability cannot be quantified due to uncertainty about the number and effect of compensable acts, both in the past and in the future, and the value of native title affected by those acts. Similarly, it is not possible to quantify the liability for compensable acts for which the Commonwealth may be directly liable.

The Commonwealth has also offered to assist the States with the costs of bodies performing native title functions under State legislation. The extent of this assistance will depend on the existence of such bodies, the timing of their recognition and the extent of their use.

Defence

HMAS MELBOURNE HMAS VOYAGER and HMAS STALWART damages claims

Former crew members of HMAS MELBOURNE have instituted legal proceedings against the Commonwealth, claiming damages for injuries allegedly caused by the HMAS VOYAGER/HMAS MELBOURNE collision on 10 February 1964. About 120 claims remain current. A number of dependency claims arising from that collision have also been made or foreshadowed by the dependants of deceased former members of the crew of HMAS VOYAGER.

Further claims are likely to be made by former members of the crew of HMAS MELBOURNE and the dependants of deceased members of the crew of HMAS VOYAGER.

A claim has also been made by a former crew member of HMAS MELBOURNE against the Commonwealth for damages for injuries allegedly sustained as a result of the HMAS MELBOURNE/USS FRANK E EVANS collision of 3 June 1969. Further claims for damages may be made by other former crew members of HMAS MELBOURNE arising out of that collision.

Three claims for damages for injuries allegedly arising out of an incident aboard HMAS STALWART that occurred on 22 October 1985 are currently the subject of legal proceedings and have yet to be finalised. It is possible that other former crew members of HMAS STALWART and the dependants of deceased members of the crew will make claims for damages arising out of that incident.

ADI Limited — officers and directors' indemnities

Under the sale agreements for ADI Limited, the Commonwealth has indemnified the directors, officers and employees for claims and legal costs associated with assistance related to the sale of the Commonwealth's shares in the company. The Commonwealth has also agreed to be responsible for the payment of the amount of any excess in respect of any claim under the policy where ADI Limited is unable to pay the excess post-sale.

Australian Submarine Corporation — indemnity provided to Electric Boat Corporation under the Process Agreement

In early 2002, the Department of Defence entered into a Process Agreement with Electric Boat Corporation (EB) to undertake a scoping exercise at the Australian Submarine Corporation (ASC) in preparation for their future Capability Partner role. For the purpose of this agreement, EB was granted a warranty that the Department of Defence had a right to disclose any information provided to EB under the Process Agreement; and an indemnity to EB against any claims brought by third parties arising out of EB's use of information provided by the Department of Defence and ASC for the purposes of the Process Agreement. EB have now concluded their scoping activity at ASC and are expected to report on their findings in mid-May.

Environment and Heritage

Newcrest Mining (WA) Limited and BHP Minerals Limited v the Commonwealth of Australia and the Director of National Parks and Wildlife

In August 1997, the High Court of Australia found that the declarations of Stage 3 Kakadu National Park in 1987, 1989 and 1991 were technically invalid with respect to 23 small areas in the south-east of the park covered by existing mineral leases held by the Newcrest group of companies. The reason for this decision was that the declaration over these areas had, with the absolute prohibition on mining activities in Kakadu under the *National Parks and Wildlife Conservation Act 1975*, effected an acquisition of property without payment of just terms compensation, as required by the Australian Constitution.

The Minister for Environment and Heritage has indicated that the lease areas need to be re-incorporated within the Park and that the Government will address the issue of 'just terms' compensation. The quantum of compensation payable for the leases and the financial consequences of incorporation of the leases into Kakadu are under active consideration. Regardless of the amount of compensation, there is an obligation for the Commonwealth to pay court costs on behalf of Newcrest. The Government has commenced negotiations with mining company representatives in relation to the extent of 'just terms' compensation.

Finance and Administration

Australian Industry Development Corporation (AIDC) — board members' and management indemnity

The Commonwealth has indemnified the Corporation's board members and management against civil claims relating to employment and conduct as directors and management of subsidiary companies. Liability is subject to the terms of the indemnities.

Australian Submarine Corporation — Commonwealth shareholding

The Commonwealth has indemnified Barry AC Hilson and BACH Pty Limited in relation to liabilities arising from assistance provided to the Commonwealth during the conduct of a review of the Commonwealth's shareholding in the Australian Submarine Corporation. This indemnity is ongoing.

Australian Submarine Corporation — directors' indemnities

The Commonwealth has indemnified the members of the Board of the Australian Submarine Corporation (ASC) for any claim associated with the provision of information to the Electric Boat Corporation of the United States. Certain information is to be provided to the Electric Boat Corporation under a Process Agreement between it, the Commonwealth and the ASC.

ComLand Limited — land remediation

The Commonwealth has indemnified the ComLand Group in the event that the Group incurs certain land remediation expenses where the need for such remediation was not identified when the land was transferred to ComLand.

Employment National Limited (EN) — board members' indemnity

Indemnities by the Commonwealth have been provided to EN board members to protect against civil claims relating to their employment and conduct as directors. These indemnities are ongoing.

Employment National Limited (EN) — letter of comfort arrangements

To protect the Government's investment in EN during the company's restructuring, a letter of comfort has been provided to the company by the Commonwealth indicating continuing financial support for the company.

Essendon Airport Limited — directors' indemnities

The Commonwealth has indemnified each member of the board of directors of Essendon Airport Limited against claims and costs incurred arising from the conduct of the directors in relation to the sale of Essendon Airport Limited. Where certain company insurances or indemnities exist for the directors in relation to a claim, the Commonwealth indemnity cannot be called upon.

Health Insurance Commission (HIC)

The Commonwealth has issued indemnities to Commissioners of the Health Insurance Commission (HIC) against claims made in connection with HIC's participation in the IT Outsourcing Initiative. The indemnity applies to actions of the members during the period of the process to outsource the HIC IT infrastructure up to the time that the HIC entered into a contract.

Indemnities for the Reserve Bank of Australia (RBA) and private sector banks

Under contractual arrangements for transactional banking services entered into by agencies covered by the *Financial Management and Accountability Act 1997*, the Commonwealth has indemnified the RBA and private sector banks against loss and damage arising out of acts or omissions by the Commonwealth, including by error, fraud, negligence or transactions made without the authority of the Commonwealth.

Sale of National Rail Corporation (NRC) Ltd

An indemnity was issued to directors and specified officers of National Rail Corporation Ltd in relation to assistance provided in the conduct of the scoping study. This indemnity was issued on 21 July 1997 and is a continuing one in respect of any liability that arises from the assistance provided before the expiry of the notice of completion from the Commonwealth.

On 20 October 2000, the Commonwealth entered into a Deed of Confidentiality with New South Wales in relation to the possible sale of NRC and FreightCorp. Under this

Deed, the Commonwealth indemnified New South Wales and the Freight Rail Corporation in relation to breach of the Deed by the Commonwealth.

The former Shareholders of NRC (the Commonwealth, New South Wales and Victoria) jointly indemnified each NRC Director against claims and legal costs incurred by that Director as a consequence of actions of the Director that related to the sale by the former Shareholders of their interests in the Company. The Deed of Indemnity is dated 3 November 2000 and provides a continuing indemnity to each Director in relation to actions covered by the Deed.

Sydney Airports Corporation Limited — directors' indemnities

The Commonwealth has indemnified each member of the board of directors of Sydney Airports Corporation Limited against claims and costs incurred arising from the conduct of the directors in relation to the sale, or scoping study for the sale, of Sydney Airports Corporation Limited. Where certain company insurances or indemnities exist for the directors in relation to a claim, the Commonwealth indemnity cannot be called upon.

Tuggeranong Office Park Pty Ltd (TOP)

The Commonwealth has provided an indemnity to the TOP Trustee to meet any shortfall in the redemption of bonds due on 20 August 2008 which cannot be sourced by TOP or the Construction Development Company (CDC) from the Sinking Fund.

Indemnities relating to other asset sales

Indemnities have been given in respect of a range of other asset sales. Details of these indemnities have been provided in previous Budget and Mid-year Economic and Fiscal Outlook (MYEFO) papers, for example see pages 10-46 to 10-51 in the 2001-02 Budget Paper No. 1.

Foreign Affairs and Trade

Export Finance and Insurance Corporation (EFIC) — board members' and senior management indemnities

The Commonwealth has provided certain indemnities to EFIC board members and senior management to protect against civil claims relating to the implementation of EFIC's alliance / divestment of its short-term export credit insurance business.

Health and Ageing

Commonwealth Serum Laboratories (CSL) Limited

CSL Limited is indemnified against claims made by persons who contract specified infections from specified products and against employees contracting asbestos-related injuries. CSL Limited has unlimited cover for most events that occurred before the sale of CSL Limited on 1 January 1994, but has more limited cover for a specified range of events that might occur during the period of the current contract. Where cover has not been arranged, the Commonwealth may have a contingent liability. Given the open-ended nature of some of the indemnities, damages and risk cannot be quantified.

Blood and blood products liability cover

The Commonwealth has signed a memorandum of understanding (MoU) with the States, Territories and the Australian Red Cross Blood Service (ARCBS) to establish a National Managed Fund (NMF). The NMF is necessary to establish a single consistent approach to pooling the liability risks associated with the supply of blood and blood products by the ARCBS within the Commonwealth of Australia. The NMF replaces previous arrangements that were on a state by state basis. The MoU provides for the parties to contribute to the NMF taking into account, inter alia, potential claims payments; the level of funds in the NMF and investment earnings; and a prudential allowance for liabilities incurred but not the subject of claims.

If there are insufficient funds to cover claim costs, the MoU provides for each party to contribute funds in accordance with allocation provisions prevailing at the time.

Under the MoU, the blood and blood products liability cover for the ARCBS is effective from 1 July 2000 and remains in force until all parties agree to terminate the arrangements from an agreed date. The MoU provides for each party to remain liable for: their share of all claims settled with the terms of the MoU including any claims made after the date of termination arising from events between the date of commencement and the date of termination; and any unresolved claims arising out of events between the commencement date and the date of termination.

Immigration and Multicultural and Indigenous Affairs

Separation of Aboriginal children from their families in the Northern Territory

Earlier laws, policies and practices in relation to the Commonwealth's administration of the Northern Territory led to the separation of certain indigenous children from their families. There are currently over 2,100 plaintiffs with claims pending against the Commonwealth for (largely unspecified) damages in relation to alleged forcible and wrongful separations (mostly by the children of those allegedly forcibly and wrongfully removed).

Only two of these claims have so far proceeded to hearing. The Federal Court in Darwin dismissed these in August 2000. An appeal to the Full Bench of the Federal Court was also dismissed in August 2001. Special leave was sought from the High Court to appeal this decision, however, this application was refused.

Industry, Tourism and Resources

Liability for damages caused by space activities

Under the United Nations Convention on International Liability for Damage Caused by Space Objects, the Australian Government is fully responsible for damages caused to nationals of other countries caused by space objects launched from, or by, Australia. The Commonwealth Government requires anyone seeking approvals under the *Space Activities Act 1998* to insure up to the level of Maximum Probable Loss (MPL), up to a maximum of $750 million per launch or return of a space object. The Commonwealth also accepts all liability caused to foreign nationals above the insured level.

Transport and Regional Services

Maritime Industry Finance Company Limited — board members' indemnity

Indemnities for Maritime Industry Finance Company Limited (MIFCo) board members have been provided to protect against civil claims relating to employment and conduct as directors of MIFCo. These indemnities are unquantifiable and no expiry date has been set.

Stevedoring Industry Finance Committee

The Stevedoring Industry Finance Committee (SIFC) faces an increasing number of claims for asbestos related injuries to former waterside workers, and a class action against SIFC was initiated in February 2001 by Slater & Gordon. These injury claims were inherited from the Australian Stevedoring Industry Authority. Costs that may arise from these claims cannot be determined and are therefore unquantifiable. The number of claims likely to be made in the future is also unknown.

Australian Maritime Safety Authority — litigation

Australian Maritime Safety Authority (AMSA) is subject to a professional negligence claim seeking unspecified damages arising from a search and rescue incident involving the loss of one life. The flotation device manufacturer and the retailer are second and third defendants. The claim is being defended, although it is not possible to estimate the amounts of any eventual payments that may result.

Australian Maritime Safety Authority — incident costs

In the normal course of operations, AMSA is responsible for the provision of funds necessary to meet the clean-up costs arising from ship-sourced marine pollution. The Commonwealth has agreed that AMSA's responsibility should be limited to a maximum expense of $10 million, and has arranged a stand-by loan facility for this purpose. The Commonwealth will provide funds in the event that costs exceed this limit. In all circumstances, the Authority is responsible for making appropriate efforts to recover the costs of any such incidents.

National codes of practice for railways — Industry Advisory Committee

Under an Inter-Governmental Agreement on Rail Operational Uniformity, an advisory committee has been formed to provide advice to the Australian Rail Operations Unit on all aspects of the development and implementation of uniform operational codes for the defined interstate rail network. The Commonwealth indemnifies members of the Advisory Committee as if they were Commonwealth employees. It is not possible to quantify the liability risk.

Tripartite Deeds relating to the sale of Core Regulated Airports

Tripartite Deeds apply to the 12 Core Regulated Airports (Sydney, Melbourne, Brisbane, Perth, Canberra, Coolangatta, Townsville, Adelaide, Hobart, Launceston, Darwin and Alice Springs). The Tripartite Deeds between the Commonwealth, the airport lessee company and financiers provide for limited step-in rights for the financiers in circumstances when the Airport Lease is terminated.

Assuming the financiers' step-in rights are not triggered, the potential liability of the Commonwealth can vary under the Tripartite Deed, depending on whether the Airport Lease is able to be sold on to a third party or not.

The Commonwealth's potential liability to the lessee's financiers is limited to the value received for the affected Airport Lease or the valuation of the airport site.

Where the Commonwealth is able to sell on the Airport Lease, secured financiers have a limited ability to recover their loans from funds obtained by the Commonwealth from selling on the Airport Lease, subject to higher ranking claims being met first.

Where the Airport Lease is not sold on, the Commonwealth is required to obtain a valuation of the airport site that will determine the limit for a repayment (or partial repayment) of financiers' loans, again subject to higher ranking claims being met first.

If the Commonwealth enters into possession of an airport site, it would seek to recover its costs from a number of sources, including airport revenues and the airport lessee Company, in addition to funds obtained from selling on the Airport Lease.

Federal Airports Corporation (FAC) — transfer of liabilities to the Commonwealth

On 24 September 1998, the Commonwealth assumed responsibility for all remaining assets, liabilities and contracts of the FAC on the wind-up of the Corporation. All of the known liabilities have been settled, however there is a risk that undisclosed liabilities remain.

Treasury

Changes in value of cross currency swaps and foreign currency denominated debt

Significant net foreign exchange gains or losses could be recorded in the AAS31 operating statement if there is a significant change in the nominal exchange rate. This is because a change in the nominal exchange rate results in a change in the net principal value of cross currency swaps and foreign currency denominated debt. The direction of movement in the exchange rate will determine whether there is a net foreign exchange gain or a loss. A gain is a positive risk to the operating result, while loss is a negative risk. Net foreign exchange gains or losses do not have any direct impact on the reported budget balances, as these are based on the Government Finance Statistics (GFS) reporting framework.

Housing Loans Insurance Corporation (HLIC) — guarantee

The Commonwealth sold the HLIC on 12 December 1997 and has assumed all residual contingencies. The principal amount covered by the guarantee and the balances outstanding are unable to be reliably measured. The guarantee relates essentially to the HLIC's contracts of mortgage insurance and any borrowings approved by the Treasurer up to the time of sale.

Part II: Sensitivity of fiscal aggregates to economic developments

A guide to the sensitivity of the forward estimates of GFS expenses and GFS revenue to variations in economic parameters in 2002-03 is provided in Table 1. It is important to recognise that such guides provide only a 'rule of thumb' indication of the impact on the budget of changes in prices, wages and other parameters. In each case, the analysis presents the estimated effects of a change in one economic variable only, and does not attempt to capture the linkages between economic variables that characterise changes in the economy more broadly.

Table 1: Sensitivity of financial aggregates to changes in economic parameters

	2002-03 $m	2003-04 $m	2004-05 $m	2005-06 $m
Expenses				
Prices	1,050	770	780	790
Wages	100	350	370	390
Unemployment benefit recipients	300	290	290	260
Safety net adjustments	60	110	180	250
Revenue				
Prices	50	100	100	100
Wages	1,410	1,520	1,620	1,740
Employment	970	1,040	1,110	1,190
Private final demand	250	260	270	270
Profit	120	200	210	230

Expenses

On the expenses side, the sensitivity analysis of the estimates provides for the following assumptions about changes to four broad groups of parameters. An increase in any of the parameters considered will lead to an increase in expenses, and a decrease in any parameters will lead to a reduction in expenses.

Prices

All price deflators are assumed to change by 1 percentage point from the beginning of the September quarter 2002, with wage deflators left unchanged.

- The effect of a change in prices is due to the indexation of Commonwealth expenses and a change in the nominal superannuation interest expense.

Wages

All wage and salary growth rates are assumed to change by 1 percentage point from the beginning of the September quarter 2002, with price deflators left unchanged.

- The effect of a change in wage and salary growth rates is largely determined by the effect of the Government's commitment to maintain selected pensions at 25 per cent of Male Total Average Weekly Earnings. The wages effect in Table 1 above does not include the effect of changes to wage and salary payments on Commonwealth departmental expenses.

Unemployment benefit recipients (includes Newstart allowance and Unemployed Youth Allowance recipients)

The total number of recipients is assumed to change by 5 per cent in the Budget year and in all the forward years.

Safety Net Adjustment

The Safety Net Adjustment (SNA) determined by the Australian Industrial Relations Commission is assumed to change by $2 per week from the beginning of the September quarter in each year.

- About $45 billion of expenses, comprising agency departmental expenses, other Commonwealth own purpose expenses and specific purpose payments to the States of a departmental expense nature, are indexed to weighted averages of movements in inflation and the SNA.

Revenue

On the revenue side, the sensitivity analysis of the estimates provides for the following assumptions about changes to five broad groups of parameters. An increase in any of the parameters considered would lead to an increase in revenue, and a decrease in any of the parameters will lead to a reduction in revenue.

Prices

All price deflators are assumed to change by 1 percentage point at the start of the September quarter 2002, with wage deflators left unchanged.

- A change in prices affects revenue primarily through changes in excise revenue.

Wages

All wage and salary growth rates are assumed to change by 1 percentage point from the beginning of the September quarter 2002, with price deflators left unchanged.

- A change in wage and salary growth rates affects revenue through changes in gross income tax withholding (ITW) and Fringe Benefits Tax (FBT) revenue.

Employment

The level of employment is assumed to change by 1 percentage point from the beginning of the September quarter 2002, with no change in the composition of employment.

- A change in employment affects revenue through increases in ITW collections.

Private final demand

The level of private final demand (consumption plus investment) is assumed to change by 1 percentage point from the beginning of the September quarter 2002, with no change in the composition of demand.

- A change in private final demand affects revenue primarily through changes in excise and customs duty collections.

Profits

The level of company profits is assumed to change by 1 percentage point from the beginning of the September quarter 2002.

- A change in the level of company profits affects revenue through changes in company tax collections.