

(Treasury, 2010:
28, 30, 51–57)

Financial Statements of the Government of New Zealand

for the year ended 30 June 2010

978-0-478-35070-8 (Print)
978-0-478-35071-5 (Online)

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978-0-478-35071-5 (Online)



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To the Readers of the Financial Statements of the Government of New Zealand for the year ended 30 June 2010

I have audited the financial statements of the Government of New Zealand for the year ended 30 June 2010, using my staff, resources and appointed auditors and their staff.

Unqualified Opinion

In our opinion, the financial statements of the Government of New Zealand on pages 28 to 164:

- comply with generally accepted accounting practice in New Zealand; and
- fairly reflect:
 - the Government of New Zealand's financial position as at 30 June 2010; and
 - the results of its operations and cash flows for the year ended on that date.

The audit was completed on 30 September 2010, and is the date at which our opinion is expressed.

The basis of our opinion is explained below. In addition, we outline the responsibilities of the Government and the Auditor, and explain our independence.

Basis of Opinion

We carried out the audit in accordance with the Auditor-General's Auditing Standards, which incorporate the New Zealand Auditing Standards.

We planned and performed the audit to obtain all the information and explanations we considered necessary in order to obtain reasonable assurance that the financial statements did not have material misstatements, whether caused by fraud or error.

Material misstatements are differences or omissions of amounts and disclosures that would affect a reader's overall understanding of the financial statements. If we had found material misstatements that were not corrected, we would have referred to them in our opinion.

The audit involved performing procedures to test the information presented in the financial statements. We assessed the results of those procedures in forming our opinion.

Audit procedures generally include:

- determining whether significant financial and management controls are working and can be relied on to produce complete and accurate data;
- verifying samples of transactions and account balances;
- performing analyses to identify anomalies in the reported data;
- reviewing significant estimates and judgements made;
- confirming year-end balances;
- determining whether accounting policies are appropriate and consistently applied; and
- determining whether all financial statement disclosures are adequate.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements.

Typically, the estimated useful lives of different classes of property, plant and equipment are as follows:

Class of PPE	Estimated useful lives
Buildings	25 to 60 years
Specialist military equipment	5 to 55 years
State highways:	
Pavement (surfacing)	7 years
Pavement (other)	50 years
Bridges	70 to 105 years
Rail Network:	
Track and ballast	25 to 40 years
Tunnels and bridges	60 to 100 years
Overhead traction and signalling	10 to 40 years
Aircraft (excluding specialist military equipment)	10 to 20 years
Electricity distribution network	2 to 80 years
Electricity generation assets	25 to 55 years
Other plant and equipment	3 to 30 years

Specified heritage and cultural assets are generally not depreciated.

Equity Accounted Investments

The applicable financial reporting standards that determine the basis of combination of entities that make up the Government reporting entity are NZ IAS 27: *Consolidated and Separate Financial Statements* and NZ IAS 28: *Investments in Associates*. NZ IAS 27 refers to guidance provided in IPSAS 6: *Consolidated and Separate Financial Statements* and FRS 37: *Consolidating Investments in Subsidiaries* which shall be used by public benefit entities in determining whether they control another entity.

These standards are, however, not clear about how the definitions of control and significant influence should be applied in some circumstances in the public sector, particularly where legislation provides public sector entities with statutory autonomy and independence, in particular with Tertiary Education Institutions. Treasury's view is that because the Government cannot determine its operating and financing policies, but does have a number of powers in relation to these entities, it is appropriate to treat them as associates.

Biological Assets

Biological assets (eg, trees and sheep) managed for harvesting into agricultural produce (eg, logs and wool) or for transforming into additional biological assets are measured at fair value less estimated costs to sell, with any realised and unrealised gains or losses reported in the statement of financial performance. Where fair value cannot be reliably determined, the asset is recorded at cost less accumulated depreciation and accumulated impairment losses. For commercial forests, fair value takes into account age, quality of timber and the forest management plan.

Biological assets not managed for harvesting into agricultural produce, or being transformed into additional biological assets are reported as property, plant and equipment in accordance with the policies for property, plant and equipment.

Intangible Assets

Intangible assets are initially recorded at cost. Where an intangible asset is created for nil or nominal consideration it is also initially carried at cost, which by definition is nil/nominal.

The cost of an internally generated intangible asset represents expenditure incurred in the development phase of the asset only. The development phase occurs after the following can be demonstrated: technical feasibility; ability to complete the asset; intention and ability to sell or use; and development expenditure can be reliably measured. Research is “original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding”. Expenditure incurred on the research phase of an internally generated intangible asset is expensed when it is incurred. Where the research phase cannot be distinguished from the development phase, the expenditure is expensed when it is incurred.

The Government’s holdings of assigned amount units arising from the Kyoto protocol are reported at fair value. Other intangible assets with finite lives are subsequently recorded at cost less any amortisation and impairment losses. Amortisation is charged to the statement of financial performance on a straight-line basis over the useful life of the asset. Typically, the estimated useful life of computer software is three to five years.

Intangible assets with indefinite useful lives are not amortised, but are tested annually for impairment.

Realised gains and losses arising from disposal of intangible assets are recognised in the statement of financial performance in the period in which the transaction occurs.

Intangible assets with finite lives are reviewed annually to determine if there is any indication of impairment. Where an intangible asset’s recoverable amount is less than its carrying amount, it is reported at its recoverable amount and an impairment loss is recognised. Losses resulting from impairment are reported in the statement of financial performance.

Goodwill is tested for impairment annually.

Non-current Assets Held for Sale and Discontinued Operations

Non-current assets or disposal groups are separately classified where their carrying amount will be recovered through a sale transaction rather than continuing use; that is, where such assets are available for immediate sale and where sale is highly probable. Non-current assets or disposal groups are recorded at the lower of their carrying amount and fair value less costs to sell.

Investment Property

Investment property is property held primarily to earn rentals or for capital appreciation or both. It does not include property held primarily for strategic purposes or to provide a social service (eg, affordable housing) even though such property may earn rentals or appreciate in value – such property is reported as property, plant and equipment.

Investment properties are measured at fair value. Gains or losses arising from fair value changes are included in the statement of financial performance. Valuations are undertaken in accordance with standards issued by the New Zealand Property Institute.

Employee Benefits

Pension liabilities

Obligations for contributions to defined contribution retirement plans are recognised in the statement of financial performance as they fall due. Obligations for defined benefit retirement plans are recorded at the latest actuarial value of the Crown liability. All movements in these liabilities, including actuarial gains and losses, are recognised in full in the statement of financial performance in the period in which they occur.

Other employee entitlements

Employee entitlements to salaries and wages, annual leave, long service leave, retiring leave and other similar benefits are recognised in the statement of financial performance when they accrue to employees. Employee entitlements to be settled within 12 months are reported at the amount expected to be paid. The liability for long-term employee entitlements is reported as the present value of the estimated future cash outflows.

Termination benefits

Termination benefits are recognised in the statement of financial performance only when there is a demonstrable commitment to either terminate employment prior to normal retirement date or to provide such benefits as a result of an offer to encourage voluntary redundancy. Termination benefits settled within 12 months are reported at the amount expected to be paid, otherwise they are reported as the present value of the estimated future cash outflows.

Insurance Contracts

The future cost of ACC claims liabilities is revalued annually based on the latest actuarial information. Movements of the liability are reflected in the statement of financial performance. Financial assets backing the liability are designated at fair value through profit and loss.

Leases

Finance leases transfer, to the Crown as lessee, substantially all the risks and rewards incident on the ownership of a leased asset. Initial recognition of a finance lease results in an asset and liability being recognised at amounts equal to the lower of the fair value of the leased property or the present value of the minimum lease payments. The capitalised values are amortised over the period in which the Crown expects to receive benefits from their use.

Operating leases, where the lessor substantially retains the risks and rewards of ownership, are recognised in a systematic manner over the term of the lease. Leasehold improvements are capitalised and the cost is amortised over the unexpired period of the lease or the estimated useful life of the improvements, whichever is shorter. Lease incentives received are recognised evenly over the term of the lease as a reduction in rental expense.

Other Liabilities and Provisions

Other liabilities and provisions are recorded at the best estimate of the expenditure required to settle the obligation. Liabilities and provisions to be settled beyond 12 months are recorded at the present value of their estimated future cash outflows.

Contingent Liabilities and Contingent Assets

Contingent liabilities and contingent assets are reported at the point at which the contingency is evident. Contingent liabilities are disclosed if the possibility that they will crystallise is not remote. Contingent assets are disclosed if it is probable that the benefits will be realised.

Commitments

Commitments are future expenses and liabilities to be incurred on contracts that have been entered into at balance date.

Cancellable commitments that have penalty or exit costs explicit in the agreement on exercising the option to cancel are reported at the value of that penalty or exit cost (ie, the minimum future payments).

Commitments are classified as:

- capital commitments: aggregate amount of capital expenditure contracted for but not recognised as paid or provided for at balance date
- non-cancellable operating leases with a lease term of more than one year, and
- other non-cancellable commitments (these may include consulting contracts, cleaning contracts and ship charters).

Interest commitments on debts and commitments relating to employment contracts are not included in the Statement of Commitments.

Comparatives

When presentation or classification of items in the financial statements is amended or accounting policies are changed voluntarily, comparative figures have been restated to ensure consistency with the current period unless it is impracticable to do so.

Comparatives referred to as Original Budget were forecasts published in the *2009 Budget Economic and Fiscal Update* while Estimated Actuals were forecasts published in the *2010 Budget Economic and Fiscal Update*. These forecasts include budget adjustments for new unallocated spending during the year (both operating and capital) and top-down adjustments which reduce the bias for forecast expenditure by departments to reflect maximum spending limits instead of mid-point estimates.

Segment Analysis

The Government reporting entity is not required to provide segment reporting as it is a public benefit entity. Nevertheless, information is presented for material institutional components and major economic activities within or undertaken by the Government reporting entity. The three major institutional components of the Crown are:

- Core Crown: This group, which includes Ministers, Departments, Offices of Parliament, the Reserve Bank of New Zealand and the New Zealand Superannuation Fund most closely represents the budget sector and provides information that is useful for fiscal analysis purposes.
- State-owned enterprises: This group includes entities governed by the State-owned Enterprises Act, and for the purposes of these statements also includes Air New Zealand Limited. This group represents entities that undertake commercial activity.
- Crown entities: This group includes entities governed by the Crown Entities Act 2004. These entities have separate legal form and specified governance frameworks (including the degree to which each Crown entity is required to give effect to, or be independent of, government policy).

Functional analysis is also provided of a number of financial statement items. This functional analysis is drawn from the *Classification of the Functions of Government* as developed by the Organization for Economic Co-operation and Development.

Related Parties

Related parties of the Government include key management personnel, and their close family members. Key management personnel are Ministers of the Crown, and their close family members are their spouses, children and dependants. Transactions between these related parties and a Government entity are disclosed in these financial statements only if they have taken place within a Minister's portfolio and they are not transactions entered into in the same capacity as an ordinary citizen.

Tertiary Education Institutions, joint ventures and the Government Superannuation Fund are also related parties of the Government due to the Government's influence over these entities. Transactions between these entities and Government entities are separately disclosed where material.

There are no other related parties as no other parties control the Government, and no other parties are controlled by the Government, other than those that are consolidated into the Government's financial statements.

The Government comprises a large number of commonly controlled entities. Transactions between these entities are eliminated in these financial statements and therefore not separately disclosed.

Transactions where the financial results may have been affected by the existence of a related party relationship are disclosed in the financial statements.

Note 2: Tax and Levies Collected through the Crown's Sovereign Power (Accrual)

Forecast			Actual	
Original Budget	Estimated Actuals		30 June 2010	30 June 2009
\$m	\$m		\$m	\$m
		Direct Income Tax Revenue (accrual)		
		Individuals		
21,699	21,884	Source deductions	21,774	22,587
4,387	4,261	Other persons	3,987	4,408
(1,651)	(1,979)	Refunds	(1,831)	(1,636)
487	459	Fringe benefit tax	461	500
24,922	24,625	Total individuals	24,391	25,859
		Corporate Tax		
7,077	6,334	Gross companies tax	6,698	8,245
(345)	(399)	Refunds	(379)	(430)
1,107	1,009	Non-resident withholding tax	884	1,451
13	(1)	Foreign-source dividend withholding payments	(3)	10
7,852	6,943	Total corporate tax	7,200	9,276
		Other Direct Income Tax		
2,049	1,812	Resident withholding tax on interest income	1,804	2,571
211	142	Resident withholding tax on dividend income	130	65
2	2	Estate and gift duties	2	1
2,262	1,956	Total other direct income tax	1,936	2,637
35,036	33,524	Total direct income tax	33,527	37,772
		Indirect Income Tax Revenue (accrual)		
		Goods and Services Tax		
21,121	19,131	Gross goods and services tax	19,797	20,551
(9,960)	(7,425)	Refunds	(7,880)	(9,000)
11,161	11,706	Total goods and services tax	11,917	11,551
		Other Indirect Taxation		
885	894	Road user charges	910	868
802	849	Petroleum fuels excise - domestic production	805	781
657	636	Alcohol excise - domestic production	600	616
172	188	Tobacco excise - domestic production	217	172
535	564	Petroleum fuels excise - imports ¹	622	514
209	234	Alcohol excise - imports ¹	225	213
840	916	Tobacco excise - imports ¹	851	891
234	219	Other customs duty	175	262
224	229	Gaming duties	219	215
167	170	Motor vehicle fees	171	171
92	68	Approved issuer levy and cheque duty	69	80
38	37	Energy resources levies	39	39
4,855	5,004	Total other indirect taxation	4,903	4,822
16,016	16,710	Total indirect taxation	16,820	16,373
51,052	50,234	Total taxation revenue	50,347	54,145
		Other Sovereign Revenue (accrual)		
3,226	3,201	ACC levies	3,261	2,880
307	304	Fire service levies	301	299
88	88	EQC levies	86	86
362	557	Child support	572	375
296	266	Court fines	238	263
581	247	Other miscellaneous items	224	215
4,860	4,663	Total other sovereign revenue	4,682	4,118
55,912	54,897	Total sovereign revenue	55,029	58,263

1. Customs excise-equivalent duty.

Note 2: Tax and Levies Collected through the Crown's Sovereign Power (Cash)

Forecast			Actual	
Original Budget	Estimated Actuals		30 June 2010	30 June 2009
\$m	\$m		\$m	\$m
Direct Income Tax Receipts (cash)				
Individuals				
21,630	21,832	Source deductions	21,744	22,567
4,983	4,745	Other persons	4,630	4,988
(2,393)	(2,739)	Refunds	(2,793)	(2,488)
487	476	Fringe benefit tax	469	506
24,707	24,314	Total individuals	24,050	25,573
Corporate Tax				
7,801	8,488	Gross companies tax	8,650	7,742
(1,379)	(1,716)	Refunds	(1,644)	(2,013)
1,106	892	Non-resident withholding tax	889	1,437
13	8	Foreign-source dividend withholding payments	6	(2)
7,541	7,672	Total corporate tax	7,901	7,164
Other Direct Income Tax				
2,051	1,778	Resident withholding tax on interest income	1,833	2,593
210	126	Resident withholding tax on dividend income	114	97
2	2	Estate and gift duties	2	2
2,263	1,906	Total direct other income tax	1,949	2,692
34,511	33,892	Total direct income tax	33,900	35,429
Indirect Tax Receipts (cash)				
Goods and Services Tax				
20,252	18,785	Gross goods and services tax	18,797	19,715
(9,360)	(7,425)	Refunds	(7,456)	(8,894)
10,892	11,360	Total goods and services tax	11,341	10,821
Other Indirect Taxation				
885	894	Road user charges	908	864
802	849	Petroleum fuels excise - domestic production	805	786
657	636	Alcohol excise - domestic production	622	587
172	188	Tobacco excise - domestic production	214	170
1,818	1,933	Customs duty	1,805	1,957
224	227	Gaming duties	218	227
167	170	Motor vehicle fees	195	165
102	75	Approved issuer levy and cheque duty	59	77
38	43	Energy resources levies	37	36
4,865	5,015	Total other indirect taxation	4,863	4,869
15,757	16,375	Total indirect taxation	16,204	15,690
50,268	50,267	Total tax receipts collected	50,104	51,119
Other Sovereign Receipts (cash)				
3,170	3,274	ACC levies	3,291	2,792
308	304	Fire service levies	301	300
88	88	EQC levies	86	87
198	197	Child support	190	177
287	172	Court fines	184	173
239	247	Other miscellaneous items	216	187
4,290	4,282	Total other sovereign receipts	4,268	3,716
54,558	54,549	Total sovereign receipts	54,372	54,835

Note 3: Sales of Goods and Services

Forecast			Actual	
Original Budget	Estimated Actuals		30 June 2010	30 June 2009
\$m	\$m		\$m	\$m
By type				
8,441	7,179	Sales of goods	7,222	7,955
-	173	Deposit guarantee schemes - guarantee fees	163	74
7,608	6,983	Rendering of services	6,946	7,327
16,049	14,335	Total sales of goods and services	14,331	15,356
By source				
1,357	1,417	Core Crown	1,387	1,237
13,858	14,086	Crown entities	14,107	13,901
13,795	11,900	State-owned enterprises	11,979	12,592
(12,961)	(13,068)	Inter-segment eliminations	(13,142)	(12,374)
16,049	14,335	Total sales of goods and services	14,331	15,356

Note 4: Interest Revenue and Dividends

Forecast			Actual	
Original Budget	Estimated Actuals		30 June 2010	30 June 2009
\$m	\$m		\$m	\$m
By type				
516	473	Student loans (interest unwind)	463	465
313	238	Other financial assets classified as amortised cost or available for sale	645	629
7	3	Financial assets classified as held for trading	3	6
1,929	2,162	Financial assets classified as fair value through profit and loss	815	1,478
2,765	2,876	Total interest revenue	1,926	2,578
394	418	Dividends	389	419
3,159	3,294	Total interest revenue and dividends	2,315	2,997
By source				
2,076	2,225	Core Crown	2,135	1,872
832	1,012	Crown entities	1,146	1,248
927	1,465	State-owned enterprises	626	771
(676)	(1,408)	Inter-segment eliminations	(1,592)	(894)
3,159	3,294	Total interest revenue and dividends	2,315	2,997

Included in total interest revenue above is interest on impaired financial assets of:

Impaired student loans	463	465
Impaired other financial assets classified as amortised cost or available for sale	4	10
Total interest revenue on impaired financial assets	467	475