



Commercial Issues

Commercial policies adopted by the Territory affect the way in which Territory Government businesses operate and the way in which the Territory Government deals with the private sector. Aspects that are relevant to the Territory Budget are:

- Government Business Division and Government Owned Corporation frameworks which recognise that business activities of Government must operate on a more commercial basis than general government agencies;
- Territory Partnerships, which outlines the framework for dealings between the Territory Government and the private sector in relation to public private partnerships; and
- the risks faced by the Territory, in particular those under contingent liabilities arising from guarantees and indemnities that the Territory has issued when dealing with the private sector and other governments.

Commercial Frameworks

Government has established legislative and administrative frameworks governing the operation of government owned businesses. The intent of such frameworks is to provide greater incentives to manage costs, increase efficiency and improve the quality of the goods and services delivered.

Typically, government owned businesses are managed according to best commercial practices in recognition that:

- their operations are similar to those of private sector businesses; and/or
- they operate in a commercial environment or in competition with private sector businesses.

Government businesses that are considered suitable to operate commercially can be declared a government business division (GBD) or a government owned corporation (GOC). Unlike general government agencies, these businesses do not receive direct output appropriation for their commercial activities. Instead, operating revenue is primarily generated from sales of goods and services to other Territory Government agencies, the private sector or a combination of both.

GBDs are subject to the financial management framework contained in the *Financial Management Act*, with the chief executive officer of a GBD accountable to the responsible Minister for financial performance.

GOCs are subject to the *Government Owned Corporations Act*, which seeks to replicate as far as possible the shareholder model of corporate governance. This structure essentially creates an 'arm's length' relationship between the GOC Board, which is responsible for management of the GOC, and the Government as owner or shareholder.

The Territory Insurance Office (TIO), another Government business, operates under its own legislative framework consisting of the *Territory Insurance Office Act* and the Territory Insurance Office Regulations. It also has a Board that is accountable for its performance. The TIO is subject to a prudential regulatory regime, similar to that applying to competitors in insurance and financial services, but administered by Northern Territory Treasury.

As part of Government's responsibilities as owner, a scoping study was commissioned to assess the longer term financial sustainability of TIO in 2005. The scoping study was finalised in March 2006 and in response, Government noted the increasing competitiveness of global insurance markets, but determined that the risks of ongoing ownership of TIO were manageable.

As such, TIO has been retained under Government ownership, with a range of reforms being undertaken to improve risk management and financial performance. These include the adoption of prudential supervision standards consistent with those applied by the Australian Prudential Regulation Authority, separate accounting and reporting of TIO's business lines, strengthened capital management and Statement of Corporate Intent processes and the establishment of the *Motor Accident (Compensation) Act* (MACA) as a separate statutory fund administered by TIO.

Government Business Divisions

The Territory has established GBDs in order to improve operating efficiency and to reduce Government and business costs, thereby freeing up Government resources for other expenditure priorities.

Commercial practices that have been implemented for GBDs are:

- full attribution of costs (including tax equivalents);
- efficient pricing based on costs;
- commercial accounting, operating under charters of operation and establishment of audit committees;
- identification and budget funding of community service obligation (CSO) payments to compensate GBDs for undertaking non-commercial activities at the direction of Government; and
- performance monitoring.

GBDs are required to comply with competitive neutrality principles which seek to ensure a level playing field with private sector counterparts and that resources controlled by GBDs are determined by relative efficiency, rather than advantages accruing as a result of Government ownership.

Competitive neutrality complaints may arise where GBDs provide services in competition with private sector businesses. Northern Territory Treasury has been charged with investigating any such complaints and advising the Treasurer and the responsible Minister of the results of such investigations. Should a complaint be upheld, the Government decides, on a case by case basis, the appropriate action to be taken in order to overcome any net competitive advantage identified by the complainant.

The current emphasis of GBD reform is to build on initiatives to date by encouraging a greater commercial focus, improved management practices, additional efficiency and productivity gains, ensuring value for money from expenditure on CSOs and more rigorous performance monitoring. Charters of operation have been reviewed to ensure that operational and commercial boundaries are appropriate in the light of market developments that have occurred since GBDs were established in the mid 1990s.



Government Owned Corporations

The *Government Owned Corporations Act* adopts the shareholder model of corporate governance. The objective of the Act is to impose capital market-type disciplines on government owned businesses and to replicate the corporate governance structures of private companies incorporated under the *Corporations Act 2001*.

Key elements of the Territory GOC framework are:

- corporations established under their own legislation but governed by an overarching legislative framework based on the Australian *Corporations Act 2001* principles;
- a commercial board of directors that is responsible for the operation of the business and accountable to the shareholding Minister for financial performance;
- a shareholding Minister (usually the Treasurer) who monitors the financial performance of the corporation;
- a portfolio Minister who monitors the service performance of the corporation and has broad industry policy responsibilities; and
- a Statement of Corporate Intent, which is essentially a performance agreement between the shareholding Minister and the GOC Board.

The shareholding Minister arrangement under the GOC framework is significantly different to the governance arrangements for general government agencies and for GBDs under the *Financial Management Act*. Under the *Financial Management Act*, the chief executive officer of a GBD is directly accountable to Government for the performance of the business. GBD Boards generally have an advisory role, with Ministers responsible for business decisions, which may or may not be taken on the advice of the Board.

Under the GOC framework, the Board is the decision-making body and is accountable for its decisions. The Board is accountable to the shareholding Minister for financial performance and to the portfolio Minister for the service quality aspects of a GOC's business.

GOCs are not subject to the *Financial Management Act*, reflecting the policy intent of operational autonomy.

The Power and Water Corporation became the Territory's first GOC on 1 July 2002 and, at this time, remains the Territory's only GOC.

The Power and Water Corporation Board is accountable for the performance of the GOC. In most of Power and Water Corporation's business lines, the corporation is subject to a regulatory regime administered by an independent economic regulator, the Utilities Commission. This regime is applicable to any party that may operate in these areas of business in the Territory.

The Minister for Essential Services is the Power and Water Corporation's portfolio Minister.

Like GBDs, the Power and Water Corporation does not receive direct budget appropriation. However, through Government agencies, it receives CSO payments for non-commercial services that it provides at the direction of Government.

Community Service Obligations

A community service obligation (CSO) arises when the Government requires a GBD or GOC to carry out activities which it would not elect to do on a commercial basis or would only do at higher commercial prices. CSOs allow the Government to achieve identifiable community or social objectives which would not be achieved if left to commercial outcomes.

Government CSO policy is aimed at clearly identifying the non-commercial functions performed by GBDs and GOCs, making the functions transparent and their delivery accountable to the community. To ensure that non-commercial functions do not affect the financial performance of the GBD or GOC, the policy provides compensation for the provision of the CSO.

The provision of CSOs through budget funding or acceptance of a lower shareholder return has two important implications:

- it enables GBDs and GOCs to manage commercial activities without having to cross subsidise non-commercial activities, promoting the development of a commercial culture within GBDs and GOCs; and
- it provides an opportunity for an annual review of those activities funded as CSOs.

CSOs are provided to the GBD or GOC by the 'purchasing' agency. Territory Government CSO-related initiatives, listed by purchasing agency for 2006-07 are presented in Table 7.1, with the following discussion on CSOs provided by the purchasing agency outlining the key components.

Tourism NT

Tourism NT provides Territory Discoveries, the Territory Government-owned tourism product wholesaler, with CSO payments to fund net costs incurred by the Northern Territory Holiday Centre in Alice Springs, specific shoulder season campaigns which assist in promoting the Territory as a year-round destination, and the inclusion of small tourism operators in its reservation system (\$0.45 million in 2006-07).

Northern Territory Treasury

Treasury allocates CSO funding to the Power and Water Corporation in accordance with Government policy regarding the provision of:

- electricity supply to domestic customers and small businesses and other organisations across the Territory at uniform tariffs (\$39.0 million in 2006-07);
- electricity supply services to tranche 4 electricity customers (primarily medium size businesses and other organisations) at a subsidised tariff (\$7.4 million in 2006-07); and
- water and sewerage services to all customers at a uniform tariff (\$5.1 million in 2006-07).

The uniform tariff CSO is not currently fully funded from the Budget. The unfunded component is met through the Power and Water Corporation earning lower profits, and Government as owner accepting lower dividends than would otherwise be the case. Conversely, the tranche 4 CSO is fully funded as this class of customer can choose their electricity supplier under the current electricity supply industry regulatory framework.

The Treasurer, as the regulatory Minister, has requested that the Utilities Commission examine a new model for determining and allocating the annual CSO payment. The new model is intended to be consistent with Council of Australian Government requirements for simple and transparent electricity subsidy structures.



Department of Health and Community Services

The Power and Water Corporation receives CSO payments to fund subsidised electricity, water and sewerage tariffs for pensioners under the Department of Health and Community Service's Pensioner Concession Scheme (\$4.1 million in 2006-07).

Department of Planning and Infrastructure

The Darwin Port Corporation (DPC) receives CSO funding from the Department of Planning and Infrastructure for non-commercial activities related to the development, operation and maintenance of wharf facilities that support the cruise ship and naval presence in the Northern Territory, the Darwin fishing and tourism industry and international trade through the Darwin Port.

It is estimated that a total of \$4.0 million in CSOs will be paid to DPC in 2006-07.

Department of Natural Resources, Environment and the Arts

The Department of Natural Resources, Environment and the Arts provides CSO funding for four non-commercial functions carried out by Territory Wildlife Parks. These functions relate to:

- maintaining the parks' assets to a high standard to assist the growth and development of the Territory's tourism industry;
- supporting the Territory's biodiversity through captive breeding of endangered, rare and threatened species;
- enhancing the education of school children by teaching them the benefits of the natural environment; and
- management of the Botanic Gardens at the Alice Springs Desert Park.

Department of Local Government, Housing and Sport

Territory Housing receives CSO payments from the Department of Local Government, Housing and Sport for non-commercial activities such as:

- rental rebates for low-income families to enable them to access secure, safe and affordable accommodation;
- providing incentives for people with medium to low incomes to increase the level of home ownership within the Northern Territory;
- rental subsidies for Northern Territory police personnel; and
- reducing up-front costs for public housing tenants purchasing their homes through the provision of a stamp duty grant.

It is estimated that a total of \$15.7 million in CSOs will be paid to Territory Housing in 2006-07. The fall in CSO funding in 2006-07 reflects the one-off nature of the \$5 million payment for Government employee housing in 2005-06.

The full range of CSOs funded by the Territory Government are detailed in Table 7.1.

Table 7.1: Community Service Obligation Payments

PURCHASING AGENCY/Provider/Description	2005-06 Estimate	2006-07 Budget
	\$000	\$000
TOURISM NT	448	448
Territory Discoveries		
Tourism Marketing	448	448
NORTHERN TERRITORY TREASURY	50 437	51 556
Power and Water Corporation		
Uniform Tariffs (electricity, water and sewerage)	43 022	44 141
Tranche 4 Customers	7 415	7 415
DEPARTMENT OF HEALTH AND COMMUNITY SERVICES	3 951	4 083
Power and Water Corporation		
Pensioner Concession Scheme	3 951	4 083
DEPARTMENT OF PLANNING AND INFRASTRUCTURE	2 284	3 981
Darwin Port Corporation		
Small Craft Services (Marine Industry Support)	274	280
Cruise and Defence (Wharf Precinct)	1 507	1 546
Tourism and Real Estate (Wharf Precinct)	473	480
Fort Hill Wharf – Roll-On Roll-Off facility (Repairs and Maintenance)		575
Fishermans Wharf – Facility (Repairs and Maintenance)		1 100
Hai Win Shipping Service (<i>MV Ursula</i>)	30	
DEPARTMENT OF NATURAL RESOURCES, ENVIRONMENT AND THE ARTS	7 817	7 834
Territory Wildlife Parks		
Territory Wildlife Park – Tourism	3 975	3 992
Territory Wildlife Park – Threatened Species	475	475
Territory Wildlife Park – Education	222	222
Alice Springs Desert Park – Tourism	2 107	2 107
Alice Springs Desert Park – Threatened Species	118	118
Alice Springs Desert Park – Education	277	277
Alice Springs Desert Park – Botanic Gardens	643	643
DEPARTMENT OF LOCAL GOVERNMENT, HOUSING AND SPORT	20 821	15 706
Territory Housing		
Rent Subsidies	13 404	13 404
Low Interest Home Loans	926	926
Fringe Benefits Tax on Employee Loans	48	48
Interest Subsidy	290	175
Stamp Duty Differential	84	84
Police Rent Forgone	1 069	1 069
Government Employee Housing	5 000	
TOTAL	85 758	83 608



Tax Equivalents Regime

GBDs and GOCs incur similar tax liabilities to privately owned organisations. This measure ensures greater parity between the cost structure of Government businesses and the private sector, aiding in the achievement of competitive neutrality. For example, the Power and Water Corporation and the Darwin Port Corporation pay local government rates equivalents to the Central Holding Authority.

It is estimated that the Power and Water Corporation will pay \$10.3 million in income tax equivalents for 2005-06 and \$14.4 million for 2006-07. The Power and Water Corporation tax expense is expected to increase consistent with a forecast increase in profitability, primarily due to higher energy costs incurred in 2005-06 not expected to continue in 2006-07, and smaller than projected fall in revenue between 2005-06 and 2006-07.

Table 7.2: Tax Equivalents

	2005-06 Estimate	2006-07 Budget
	\$000	\$000
Income Tax Equivalents from GBDs		
Northern Territory Treasury Corporation	7 233	7 138
Darwin Bus Service	15	34
Construction Division		427
Data Centre Services	361	275
Government Printing Office	170	55
NT Fleet	2 113	2 162
Total Tax Equivalents from GBDs	9 892	10 091
Income Tax Equivalents from GOCs		
Power and Water Corporation	10 281	14 368
Local Government Rates Equivalents from GBDs		
Darwin Port Corporation	156	160
Local Government Rates Equivalents from GOCs		
Power and Water Corporation	179	183
Total Tax Equivalents	20 508	24 802

Note: GBDs not shown paid no tax in 2005-06 and are not expected to in 2006-07.

Dividend Policy

If the Treasurer is satisfied that a GBD or GOC has sufficient resources, it may be determined that the GBD or GOC is to pay a dividend to the Government. Generally, the Territory Government's primary benchmark is an ordinary dividend of 50 per cent of after-tax profit. However, a dividend payout ratio of 50 per cent may not always be appropriate, particularly where:

- a GBD's or GOC's debt levels are unsustainable in the medium to long term;
- where a GBD or GOC has significant future capital expenditure needs; or
- Government elects to receive a lesser amount due to CSO obligations.

The Board of a GOC is to declare the amount of a dividend on the shares of a GOC, but the shareholding Minister may direct the Board of a GOC to declare a special dividend.

Special dividends can be declared where there are sufficient resources to pay an extra amount. An example is the Northern Territory Treasury Corporation, which operates as the Government's Central Financing Authority. The corporation generates its revenue from the positive margin between lending and borrowing activities. As the corporation does not need to retain profits to meet capital costs, it is appropriate for it to pay a dividend of 100 per cent of after-tax profit.

Dividends payable by GBDs and GOCs are projected at \$36.9 million in 2006-07, an increase of \$5.1 million from 2005-06. Increased dividend income is primarily due to the forecast increase in Power and Water Corporation profitability.

The Power and Water Corporation's projected dividend in 2006-07 is \$16.8 million, 50 per cent of its net profit after tax. This profit level is reached after the payment by the Territory of the \$55.6 million CSO to be paid in 2006-07. The dividend is expected to increase in 2006-07, consistent with a forecast increase in profitability.

Table 7.3: Dividends Payable to Government

	2005-06 Estimate	2006-07 Budget
	\$000	\$000
Dividends from GBDs		
Northern Territory Treasury Corporation	16 877	16 655
Darwin Bus Service	18	40
Construction Division		498
Data Centre Services	421	321
Government Printing Office	199	65
NT Fleet	2 465	2 522
Total Dividends from GBDs	19 980	20 101
Dividend from GOC		
Power and Water Corporation	11 790	16 763
Total Dividends to Government	31 770	36 864

Public Private Partnerships

Public private partnerships (PPP) is a term used to describe a method of procuring Government infrastructure and associated services. PPPs create opportunities with the private sector for increasing investment in social and economic infrastructure, and the Territory's PPP policy framework, Territory Partnerships, defines the protocol for such commercial dealings between the public and private sectors.

Generally projects considered for PPP arrangements are those with significant whole of life costs (generally greater than \$50 million in today's dollars) and which are long term in nature (20 to 30 years). Usually a PPP project will be attractive to the private sector, where it presents a viable commercial business opportunity. A commercial opportunity is more likely to be created where third party revenues are available (such as from road tolls on a roadway) or where economies of scale can be achieved in construction and ongoing maintenance (such as with a group of schools).



From the Government's perspective, value for money will be achieved where there is private sector experience and expertise in delivery of the project and there is an environment of competitive tension to deliver the best outcome for Government. To achieve this, a PPP requires a rigorous and structured project development and evaluation process which assists in allocation of risks to the party best able to manage them. With these elements present, the bidding process will help ensure that efficient and optimal risk transfer occurs at realistic cost and that service delivery and innovation are maximised.

The Territory formally released its Territory Partnerships framework in April 2004. In line with a move by all governments in Australia towards uniform policy in this area, the policy is largely based on the policies of both the Victorian and New South Wales governments. The Territory Partnerships framework is premised on:

- the primary decision-making criteria as to whether to pursue a PPP being value for money and whether the project is considered to be in the public interest;
- all potential PPP projects require development of a public sector cost benchmark or comparator;
- projects of sufficient scale (\$50 million net present value whole of life costs would generally be the minimum size) and duration;
- projects with capacity for optimal risk allocation between the public and private sectors;
- projects which allow scope for innovative solutions from the private sector;
- projects which provide a genuine business opportunity for the private sector; and
- projects which foster a competitive bidding environment.

In progressing a uniform Australia-wide approach to PPPs, the Territory is represented on a National Ministerial Forum which focuses on fostering and promoting a national PPP market.

The Territory's first project under the Territory Partnerships framework is the Darwin Convention and Exhibition Centre (the Convention Centre) component of the Darwin Waterfront Development. This project involves the redevelopment of some 25 hectares of waterfront land in Darwin and the construction and long-term operation of the Convention Centre, as well as residential and commercial components.

Darwin Waterfront Development

The Darwin Waterfront Development is a significant initiative developed by the Northern Territory Government under its Territory Partnerships policy for public private partnerships. This project will combine substantial community infrastructure, the Convention Centre, a serviced apartment hotel and residential accommodation. It will be linked to Darwin's central business district via pedestrian access to Smith Street. The development will provide economic opportunities as well as recreational and social opportunities for Territorians and visitors to the Top End. The Territory Government's financial contribution for the community infrastructure and the Convention Centre through a public private partnership has resulted in a \$1.1 billion project that will deliver long term economic and social benefits to the Northern Territory.

At the time of the May 2005 Budget, the Darwin Cove Consortium had been selected as the preferred proponent for the redevelopment and negotiations were being finalised for the commercial relationship with the consortium.

Financial close subsequently occurred on 9 May 2005, and involved separate transactions with individual consortium developers including a Concession Deed for the Convention Centre and separate Project Delivery Deeds for the community infrastructure, hospitality and residential components.

Consortium developers and major contractors are as follows:

Convention Centre Concession Holder	Darwin Cove Convention Centre Pty Ltd
Community Infrastructure Developer	Darwin Cove Convention Centre Pty Ltd
Convention Centre Design and Construction	Sitzler Barclay Mowlem Joint Venture
Hospitality Developer	DCW Hospitality Pty Ltd
Community Infrastructure Design and Construction	Macmahon NT
Convention Centre Operator	Ogden IFC (Darwin) Pty Ltd
Convention Centre Facilities Management	Honeywell Ltd
Residential Developer	Toga Darwin No1 Pty Ltd

The following three elements are key to the transaction:

(1) Darwin Convention and Exhibition Centre

- The concession holder is required to finance, design, construct, provide ongoing maintenance and operate the Convention Centre for 25 years, with the design and construct contractor Sitzler Barclay Mowlem Joint Venture taking design and construction risk. Honeywell Ltd will maintain the Convention Centre for 25 years and Ogden IFC (Darwin) Pty Ltd will be the Convention Centre operator. Currently the foundation pad for the Convention Centre is complete and construction of the building itself will continue in 2006-07.
- The Territory will make payments over 25 years for the Convention Centre that include capital, maintenance, operating cost and incentive-based components. The operating arrangements will be reviewed on an annual basis to take into account actual performance. The arrangements include incentives to maximise the growth in convention delegate numbers.
- Payments can be abated or suspended if the Convention Centre is not maintained to appropriate standards or the consortium is in breach of its obligations.

(2) Community Infrastructure

- The community infrastructure includes a sea wall, extensive boardwalks, water recreation areas, swimming facilities, wave lagoon, a new cruise ship terminal at Fort Hill Wharf and connections to Darwin's central business district. Currently, work has commenced on the sea wall with more than 340 metres already in place.
- The community infrastructure developer will design and construct the community infrastructure with the design and construct contractor Macmahon NT taking on design and construction risk. Ownership of the community infrastructure will transfer as aspects are completed through to 2008. Some aspects will be handed over later than originally contemplated under the project delivery deed and is intended to coincide more closely with completion of the Convention Centre.
- The Territory will establish a statutory authority to manage the overall site, including the community infrastructure.

(3) Property Development

- The consortium will develop the commercial aspects of the site over time and in accordance with market demand. The arrangements will ensure that stage 1 of the property development will be delivered shortly after the Convention Centre is complete, and include an apartment hotel to complement the Convention Centre and about 138 residential units and commercial and retail space.
- The remaining property development stages (totalling about 1300 apartments for both stages) will be delivered over time in accordance with market demand. It is expected that the full development of the site will occur over 15 years.
- The consortium will also be responsible for providing community infrastructure to the remaining property development stages.

Financial Implications

The redevelopment of the 25 hectare site has an estimated value on completion of \$1.1 billion. The majority of the construction costs will be invested by the Darwin Cove Consortium.

The Territory has responsibility for making operational payments for the Convention Centre over 25 years and during construction for the stage 1 community infrastructure. The Territory will share in the property returns from the development of all stages as they occur, thus taking advantage of increased property prices.

The total net cost to the Territory in today's dollars, after taking into account all costs and revenues over the life of the project, is estimated at between \$118 million and \$144 million.

At the time of the May 2005 Budget, the forecasts in the Budget Papers were based on the best estimate available with reference to negotiations at that time. In the 2005-06 Mid Year Report, the forecasts were updated to incorporate the transactions following financial close. In the formulation of the 2006-07 Budget, the forecasts have again been updated to take into account revised timing for the community infrastructure to better coincide with completion of the Convention Centre. A minimal change in timing of the Convention Centre has also been estimated between 2005-06 and 2006-07. While overall the total cost is the same, Table 7.4 shows the effect between years of the revised timing of the community infrastructure.

Table 7.4: Timing of Payments for Community Infrastructure

	2004-05 Actual	2005-06 Estimate	2006-07 Budget	2007-08 Forward Estimate	Total
	\$000	\$000	\$000	\$000	\$000
Budget	5 033	55 694	36 373		97 100
Revised Estimate	3 750	36 350	38 087	18 913	97 100
Variation	-1 283	-19 344	1 714	18 913	

The risks in relation to the Darwin Waterfront Development project relate to discriminatory changes in law, native title and environmental clean-up costs. The amount of these risks is unable to be estimated accurately but provision has been made in the forward estimates for environmental clean-up costs and it is within the Territory's discretion whether to make a discriminatory change in law.

Commercial Risks in Relation to the Budget

This section outlines risk issues that relate to formulation of the budget and the performance of the public sector against the budget. All forecasts are subject to a degree of risk and therefore some risk attaches to the Budget and forward estimates.

The Budget and forward estimates have been developed based on a range of factors about which consensus exists at the time the Budget is framed. However, events occurring after the Budget has been tabled may affect actual Budget outcomes in current and future years.

In addition to changes in economic or other parameters, such as inflation rates, interest rates and exchange rates, factors which may affect the budget outcome result from the commercial relationships and dealings between the Territory Government and other governments or the private sector. These encompass matters such as the exclusion of certain items from forecasts because of uncertainty about timing, and possible crystallisation of contingent liabilities.

In any discussion about the Budget, it is important to consider that the largest source of revenue for the Territory Government is goods and services tax (GST) revenue paid by the Australian Government. Although it is expected that national GST collections will grow over time, the revenue base is subject to volatility associated with economic cycles. Additionally, the recommendations of the Commonwealth Grants Commission are of greater importance to the Territory than for other jurisdictions because of the Territory's greater reliance on GST revenue, and they therefore pose greater risks to the Territory than to other jurisdictions. Further discussion on the risks to GST revenue estimates is provided in Chapter 5 of this Budget Paper.

Contingent Liabilities

A contingent liability is a liability that the Government may be called on to meet at some future date if a specified event should occur. Contingent liabilities of the Territory may arise out of a range of circumstances, the most common of which are indemnities and guarantees contained in agreements executed by the Territory. Contingent liabilities may also arise as a result of undertakings made by the Territory or as a result of legislation containing a guarantee or indemnity.

Details of estimated amounts of material contingent liabilities at 30 June 2005 resulting from guarantees or indemnities granted by the Territory are presented in Table 7.5.

Table 7.5: Material Quantifiable Contingent Liabilities

	Estimated Quantifiable Contingent Liability at 30 June 2005
	\$M NPV ¹
Amadeus Basin to Darwin Gas Pipeline	230
Pine Creek/McArthur River Electricity Purchase Agreements	94
Public Trustee Common Fund	29

¹ Future values discounted at a nominal 7 per cent discount rate.



Material contingent liabilities of the Territory are defined as guarantees and indemnities with potential exposure greater than \$5 million and are disclosed in annual financial statements of the Territory in accordance with Australian Accounting Standards requirements. Quantifiable and unquantifiable material contingent liabilities of the Territory are outlined below.

Quantifiable Contingent Liabilities

Electricity, Gas and Water Supply

These contingent liabilities result from arrangements for the purchase and transportation of gas, and the purchase and sale of electricity by and for the Power and Water Corporation. Material contingent liabilities relating to these arrangements are reported below.

The Power and Water Corporation has been a government owned corporation (GOC) since 1 July 2002. Under the *Government Owned Corporations Act*, a GOC is not within the shield of the Crown and the obligations of a GOC are not guaranteed by the Territory except where the Treasurer specifically agrees to this. The following Territory commitments were given prior to the Power and Water Corporation (formerly the Power and Water Authority) becoming a GOC and will remain in place until the relevant contractual arrangements cease.

Amadeus Basin to Darwin Gas Pipeline

The Territory indemnified the company which constructed the natural gas pipeline from the Amadeus Basin to Darwin in support of obligations of the Power and Water Corporation to the company. The Territory also supported the corporation's financing obligations to the pipeline company and its financiers. Should this facility be terminated prior to the end of the contract term, the Territory undertook to stand behind and, if necessary, underwrite the refinancing of the outstanding facility amount including a lease residual due to be paid at the end of the facility term. The lease residual at the end of the contract term is a direct contingent liability of the Territory unrelated to any obligation of the Power and Water Corporation.

The Territory guaranteed gas producers in support of the obligations of a subsidiary company of the Power and Water Corporation under gas purchase contracts and provided a letter in support of a loan to the corporation's subsidiary company used to meet the company's development obligations under a gas purchase agreement.

In the event that the Power and Water Corporation experienced a significant decline in its sales of electricity, there is a risk that the corporation may have a lesser requirement for natural gas to be delivered through the Amadeus Basin to Darwin gas pipeline. In circumstances where the decline was severe, both gas purchase contracts and the pipeline financing arrangements could present a risk to the corporation and the Territory, as there would be ongoing payments made despite reduced need for delivered gas. This situation is considered highly improbable.

On the other hand, there is a risk that contracted supplies of gas will prove inadequate to meet the fuel needs for a public electricity supply. Although most installed capacity that generates electricity for public supply can use alternative liquid fuels, there is presently a very significant price differential between gas and liquid fuels at all locations where gas can be delivered through existing infrastructure.

The Power and Water Corporation has advised that it expects to be able to meet its needs and those of the public electricity market for at least the next five years. Within this timeframe, the corporation is planning to contract for additional gas supplies, most likely from one of the gas fields located in waters adjacent to the Top End of the Territory. Risks related to gas supply shortfall are not associated with guarantees or indemnities in contracts, as they relate to situations where existing contracts cannot meet the corporation's needs.

Electricity and Gas Supply to Pine Creek and McArthur River

The Power and Water Corporation has entered into agreements for the provision of gas and wholesale supply of electricity for the supply of power to the Pine Creek region and McArthur River Mine. The agreement for the supply of gas contains three indemnities relating to the Power and Water Corporation supplying non-conforming gas. The corporation's contingent liability is unquantifiable. However, a major portion of the value of the contingent liability is the cost of overhauling turbine machinery owned by the electricity producers, where damage has been caused by the provision of non-conforming gas. Since 5 March 2003, no gas has been supplied to the power stations, significantly reducing, but not entirely removing, the risk exposure.

Under the Power and Water Corporation's current operating practices, the contingent events relating to each of the above indemnities are within the corporation's control and are expected to be easily avoidable.

In relation to the electricity purchase agreements, the Territory has provided an indemnity against possible actions of the Territory in relation to the structure or operations of the Power and Water Corporation. The Territory's maximum exposure is equivalent to the net present value of lease and operating charges under the purchase agreements. This risk is within the Territory's control.

Transport

Contingent liabilities in this category relate to indemnities and guarantees that have been provided in support of the Adelaide to Darwin railway project.

The AustralAsia Railway Corporation (AARC) and the Northern Territory and South Australian governments have entered into a concession arrangement for the Adelaide to Darwin railway on a build, own, operate and transfer-back basis.

Quantifiable contingent liabilities of the Territory identified in previous years in relation to the project arose from commitments to provide a capped amount of \$25 million in contingent equity, of which 50 per cent will be provided by the Australian Government. The equity was fully called and paid in June 2005.

Unquantifiable Contingent Liabilities

Unquantifiable contingent liabilities exist which could pose a risk to the Government's financial projections.

Transport

Unquantifiable contingent liabilities of the Territory in relation to the Adelaide to Darwin railway project relate to the following:

- joint guarantee of the obligations of the AARC;
- indemnities granted in relation to title over the railway corridor (title is secure but the indemnity continues);
- agreement to compensate in the case of early termination of the project (where a termination event is caused by the Territory); and



- indemnities in favour of the Australian Government for its financial contribution.

The Darwin Port Corporation has leased facilities at the Darwin Port to Asia Pacific Transport Pty Ltd, interfacing the port and the railway. There are contingent liabilities which arise out of the performance of the facilities.

Although the majority of contingent liabilities arising from the above guarantees and indemnities are unquantifiable, AARC and the governments have comprehensive risk management procedures in place for all events that would give rise to liabilities.

The Northern Territory Government has entered into agreements for the relocation of fuel terminals from near the Darwin central business district to the East Arm industrial estate. The agreements provide for certain unquantifiable contingent liabilities to be provided to the developer of the new fuel terminal and an oil company. Government has put in place comprehensive risk management processes to address potential exposure.

Health and Community Services

The Territory has granted a series of health-related indemnities for various purposes including indemnities to specialist medical practitioners employed or undertaking work in public hospitals and indemnities provided to medical professionals requested to give expert advice on inquiries before the Medical Board. Indemnities have also previously been granted to midwives.

Although the risks associated with health indemnities are potentially high, the beneficiaries of the indemnities are highly trained and qualified professionals. The indemnities generally cannot be called upon where there is wilful or gross misconduct on the part of the beneficiary.

Government Administration

Where the Territory has invited the participation of private sector persons and Government officers on boards of government owned or funded companies or corporations, the Territory may grant an indemnity to board members, which covers them for any losses that may result from good faith actions. This indemnity is generally consistent with the cover available through directors' and officers' insurance, and the policy of issuing an indemnity rather than purchasing commercial insurance is in line with the Government's policy of self insurance.

The resulting contingent liabilities are considered low risk as board members are professionals selected on the basis of their expertise and knowledge. Further, the indemnities are restricted to good faith actions only.

Indemnities are granted to the Australian Government and other entities involved in funding or sponsoring activities and programs initiated or undertaken by the Territory. Under the indemnities, the Government generally accepts liability for damage or losses occurring as a result of the activities or programs and acknowledges that, while the Australian Government or another party has contributed financially or provided in-kind support, the Territory is ultimately liable for the consequences of the activity or program.

Although the resulting contingent liability may not always be low risk, depending on the activity undertaken, the Territory's financial exposure is no greater than would have been the case without funding or sponsorship assistance.

The Government has indemnified private sector insurers providing workers' compensation insurance in the Territory. The indemnity covers insurers for losses which may arise as a result of acts of terrorism. It is considered unlikely that the indemnity will be called, notwithstanding that the consequence in terms of financial exposure, should the indemnity be called, is potentially significant.

The Territory Government generally self insures its insurable risk. The size of the Government budget, coupled with the spread of risk, the small size and high degree of centralisation of Government activities, have been considerations in determining that self insurance is appropriate. Government's primary exposure is to natural disaster risks that are outside Government control, for example, cyclones. In previous years, where catastrophic natural disasters result in major loss, the Australian Government has provided assistance, even beyond the terms of the Natural Disaster Relief Arrangements.

Finance The Territory's financial management framework is underpinned by centralised banking arrangements. The sole provider of banking-related services has been granted indemnities under the whole of government banking contract. These indemnities are considered not to involve significant risk.

Property and Business Services Agreements for leases or licences of property, plant or equipment generally contain standard indemnity provisions covering the lessor or licensor for any losses suffered as a result of the lease or licence arrangement. These indemnities are considered not to involve significant risk.

Potential contingent liabilities arising from the Darwin Waterfront Development are covered above.

Statutory Contingent Liabilities

A number of material statutory contingent liabilities also exist, however, the prospect of these contingent liabilities being called upon is considered negligible.

Public Trustee Act Under section 97 of the *Public Trustee Act*, the Treasurer indemnifies the Common Funds against any deficiencies in money available to meet claims on it. The Common Funds are a repository for all moneys received by the Public Trustee on behalf of estates, trusts or persons, and earns interest. Money to the credit of the Common Funds is invested according to the directions issued by an Investment Board.

Negotiations Not Yet Finalised Negotiations not yet finalised have the capacity to influence the achievement of budget projections and have the potential to affect both revenue and expenses, as well as the Balance Sheet.

However, as indicated above, the Budget and forward estimates have been developed based on a range of factors about which consensus exists at the time the Budget is framed.

Legal Proceedings Like negotiations not yet finalised, the outcome of legal proceedings brought by and against the Government also have the potential to affect actual Budget outcomes in current and future years. The Budget and forward estimates have been developed based on consensus existing at the time the Budget is framed.