

CHAPTER 7 – CONTINGENCIES AND LIABILITIES

CONTINGENT ASSETS

A contingent asset is a possible asset that arises from past events, whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.

These can be classified into either quantifiable, where the potential economic benefit is known, or non-quantifiable. Table 7.1 contains quantifiable contingent assets as at June 2008 and a revised estimate of these contingent assets as at June 2009.

Quantifiable contingent assets

Table 7.1: Quantifiable contingent assets

	<i>(\$ million)</i>	
	<i>As at June 2008</i>	<i>Estimate for June 2009</i>
Guarantees, Indemnities	1.3	2.0
Legal proceedings and disputes	3.3	3.3
Other ^(a)	112.1	78.5
Total contingent assets	116.7	83.9

Source: Department of Treasury and Finance

Notes:

(a) Other includes the EastLink project of \$49 million. The remaining amounts in Other relate to smaller individual contingencies.

EastLink

The EastLink Concession Deed provides for staged reductions in the amount of the Construction Bond at certain milestone dates. The first of these reductions was prescribed to occur on the date which was one month after the last Date of Tolling Completion, which occurred on 13 June 2008. Accordingly, the Construction Bond was reduced by 50 per cent from \$88 million to \$44 million (as required by the Concession Deed) on 13 July 2008. The Operation Phase Bond, in the sum of \$5 million, does not reduce.

Non-quantifiable contingent assets

City Link compensable enhancement claims

The Melbourne City Link Concession Deed contains compensable enhancement provisions that enable the Victorian Government to claim 50 per cent of additional revenue derived by City Link Melbourne Limited as a result of certain events that particularly benefit City Link, including changes to the adjoining road network.

On 20 May 2005, the Victorian Government lodged a compensable enhancement claim relating to works to improve the traffic flow on the Westgate Freeway between Lorimer and Montague Streets.

On 29 September 2006, the Victorian Government lodged a compensable enhancement claim relating to works to improve the traffic flow in the vicinity of the intersection of Bulla Road and the Tullamarine Freeway.

Under the Monash Westgate Freeways Improvement project, the Victorian Government's share of revenue uplifts will be calculated and paid three years after the completion of the project.

Channel Deepening Project Environmental Performance Bond

On 14 December 2007, the Minister for Environment and Climate Change approved the Channel Deepening Project under the *Coastal Management Act 1995*. The approval was subject to a number of conditions, including the Port of Melbourne Corporation providing a \$100 million environmental performance bond. The potential impact from this arrangement is that, in the event the bond is called upon, the Minister for Environment and Climate Change (being the beneficiary of the bond) will receive funds up to an amount of \$100 million, which are to be used for remedial or recovery works as agreed with the Minister for Roads and Ports.

EastLink

On 14 October 2004, the State entered into a concession deed with ConnectEast to design, construct, finance and operate EastLink. In addition to the quantifiable contingent assets listed earlier, there is a non-quantifiable contingent asset relating to the Hand Over Bond through which ConnectEast has an obligation to the State, in certain limited circumstances, to cover project rectification costs to the end of the concession period in 2043.

CONTINGENT LIABILITIES

A contingent liability is:

- a possible obligation that arises from past events, whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
- a present obligation that arises from past events but is not recognised because:
 - it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or
 - the amount of the obligation cannot be measured with sufficient reliability.

As with contingent assets, contingent liabilities are also classified as either quantifiable or non-quantifiable. Table 7.2 contains quantifiable contingent liabilities as at June 2008 and a revised estimate of these contingent liabilities as at June 2009.

Quantifiable contingent liabilities

Table 7.2: Quantifiable contingent liabilities

	<i>(\$ million)</i>	
	<i>As at June 2008</i>	<i>Estimate for June 2009</i>
Guarantees, Indemnities	338.4	366.5
Legal proceedings and disputes	349.9	349.3
Other	182.9	188.5
Non-general government debt ^(a)	4 516.5	7 203.9
Total contingent liabilities	5 387.7	8 108.1

Source: Department of Treasury and Finance

Note:

- (a) *Represents guarantees by the GG sector to agencies in the public non-financial corporations sector (primarily the water entities and other non-GG sector entities) for loans. The increase since June 2008 is due mainly to increased water sector capital works funded from borrowings.*

Non-quantifiable contingent liabilities

A number of potential obligations, which are non-quantifiable at this time, have been recognised by the Government arising from:

- indemnities provided in relation to transactions, including financial arrangements and consultancy services, as well as for directors and administrators;
- performance guarantees, warranties, letters of comfort, and the like;
- deeds in respect of certain obligations; and
- unclaimed moneys which may be subject to future claims by the general public against the State.

An overview of the more significant non-quantifiable liabilities follows.

2009 Victorian Bushfires

In February 2009, devastating fires ravaged many parts of Victoria. These fires have impacted significantly on local communities and have required the application of material resources by the State to assist with the fire suppression, recovery and reconstruction of the affected areas, with the Commonwealth Government agreeing to jointly fund relevant programs. The Victorian Government has announced the establishment of the Victorian Bushfire Reconstruction and Recovery Authority to coordinate the activities of Local, State and Commonwealth Government agencies, and the communities involved, to assist with recovery and rebuilding activity across Victoria. While a significant quantum of expenditure has been included in the *2009-10 Budget Papers*, as at the date of the publication of this report, the full financial impact of this catastrophic event on the State of Victoria is yet to be quantified.

Asset sales

Potential exposures are associated with the sale of a number of assets and services where the purchaser was provided with various indemnities and warranties.

Royal Melbourne Showgrounds

A contingent liability exists relative to any claims which may be made against the Showgrounds Nominees Pty Ltd arising in relation to joint venture dealings as outlined in the Development and Operations Agreement for Royal Melbourne Showgrounds. An undertaking has been given by the joint venture parties to meet the indexed service fees payable to the concessionaire (developer) under the Development and Operations Agreement as and when they fall due, subject to the concessionaire's achievement of defined service standards at the showgrounds and relevant abatement if there are service failures.

Under the State Support Deed – Core Land, the State undertakes to ensure the performance of the payment obligations in favour of the concessionaire and the performance of the joint venture financial obligations in favour of the security trustee.

Under the State Commitment to the Royal Agricultural Society (RAS), the State has agreed to support certain obligations of the RAS which may arise out of the Joint Venture Agreement. In accordance with the terms in the State Commitment to the RAS, the State will meet certain RAS obligations, in the form of a loan, if requested by the RAS when the RAS does not have financial capacity to pay, and provided the RAS has materially complied with all its material obligations under the Project Objectives Agreement, RAS Events Agreement and other Joint Venture project documents. If any outstanding loan amount remains unpaid at a date which is 25 years after the commencement of the operation term under the Development and Operation Agreement (commencement being 24 August 2006), the RAS will be obliged to satisfy and discharge each such outstanding loan amount. This may take the form of the transfer to the State of part or the whole of the RAS' participating interest in the joint venture.

The State has also entered into an agreement through the State Support Deed – Non-Core Land with Showgrounds Retail Developments Pty Ltd and the RAS whereby the State agrees to support certain payment obligations of the Royal Agricultural Society of Victoria Limited that may arise under the Non-Core Development Agreement. This agreement concerns the development of a non-core site on Epsom Road involving construction of a supermarket, shops and child care centre. In March 2007, Showgrounds Retail Developments Pty Ltd subsequently assigned all its rights and obligations under these agreements, via an Assignment Deed, to Coles Group Property Developments Ltd.

National Electricity Code Administrator

As part of the wind up of the National Electricity Code Administrator (NECA), the State has undertaken to indemnify the actions of the NECA Directors for a period of seven years upon completion of their tenure.

Public transport rail partnership agreements

The Director of Public Transport (the Director), on behalf of the Crown, entered into revised partnership contractual arrangements with franchisees to operate rail transport services in the State, operative from 18 April 2004 to November 2009. The following summarises the major contingent liabilities arising from those arrangements.

Contingent liabilities on early termination or expiry of franchise agreement

Franchise assets: to maintain continuity of services, the Director, at early termination or expiry of the franchise agreement, will either purchase the assets or have the assets transferred to the successor.

Unfunded superannuation: at the early termination or expiry of the contract, the Director will assume any unfunded superannuation amounts (apart from contributions the franchisee is required to pay over the contract term) to the extent that the State becomes the successor operator.

National Express receivership

In December 2002, the Government appointed receivers and managers to the National Express train and tram franchises, in order to protect government interests, ensure continuation of services up to the commencement of new franchise agreements, and deal with any subsequent termination issues.

The Treasurer, under the Receivership Deed of Indemnity, has agreed to indemnify the receivers for debts properly incurred by them in the course of receivership. The Treasurer has also agreed to remunerate the receivers in accordance with the rates set out in the deed.

Melbourne City Link

An outstanding claim exists from Transurban City Link Limited, pursuant to the Melbourne City Link Concession Deed, relating to an alleged Material Adverse Effect in respect of the construction of Wurundjeri Way. Expert determination found in favour of the State. However, the claim has now been appealed to arbitration, which is currently proceeding. VicRoads is defending this claim and is unable to assess the likelihood of success at this time.

EastLink

On 14 October 2004, the State entered into a Concession Deed with ConnectEast to design, construct, finance and operate EastLink. The major non-quantifiable contingent liability arising from the concession deed relates to the Key Risk Management Regime. The regime relates to the occurrence of certain circumstances that may have a detrimental impact on the concessionaire's ability to achieve its forecast returns. It identifies the areas that enable the concessionaire to claim redress from the State. These may include acts of prevention, failure to support a principal road interface, changes in State law, native title and the environmental effects statement.

Native Title

A number of claims have been filed with the Federal Court under the *Native Title Act 1993 (Cwth)* that affect Victoria. While many such claims are being processed through the legal system, the Government has committed itself to resolving claims through mediation, where possible. It is not feasible at this time to quantify any future liability.

Department of Education and Early Childhood Development

Contractual and funding arrangements entered into by the Department of Education and Early Childhood Development with the Commonwealth, State departments and non-government entities may provide for indemnities, the scope of which are negotiated on a project-by-project basis in accordance with the risk associated with the individual project.

Indemnities are provided by Department of Education and Early Childhood Development to teachers, volunteer workers, school chaplains and school councils. This indemnity for teachers protects them against liability for personal injuries to students provided the teacher was not intoxicated, or engaged in a criminal offence, or engaged in outrageous conduct, and was incurred in the course of the teacher's employment.

Indemnities are provided by Department of Education and Early Childhood Development to members of school councils. The *Education and Training Reform Act 2006* provides a comprehensive indemnity to members of school councils for any legal liability, whether in contract, negligence, and defamation, etc.

The Government also provides an indemnity for persons employed under the *Public Administration Act 2004*.

HIH Insurance

The State's quantifiable direct exposures arising from the collapse of the HIH Insurance Group (HIH) are included in the liabilities shown in the financial statements of the entities directly responsible for them. The State's obligations in respect of its builders' warranty insurance rescue package are also shown as direct liabilities of the relevant government entities.

The State also retains some unquantifiable contingent exposures arising from the collapse. These contingent exposures arise primarily through the possibility that the State may be involved in litigation in which it would be entitled to recover damages from third parties. If these third parties were insured by HIH, recovery in full may not be possible.

Land remediation – environmental concerns

In addition to properties for which remediation costs have been provided in the State's financial statements, certain other properties have been identified as potentially contaminated sites. The State does not admit any liability in respect of these sites. However, remedial expenditure may be incurred to restore the sites to an acceptable environmental standard.

Victorian Managed Insurance Authority – Insurance Cover

The Victorian Managed Insurance Authority (VMIA) was established in 1996 as an insurer for departments and participating bodies (predominantly in the general government sector). VMIA provides its client bodies with a range of insurance cover, including for property, public and products liability, professional indemnity and contract works. VMIA re-insures in the private market for losses above \$50 million arising out of any one event, up to a maximum for each type of cover (e.g. \$1 250 million for property and \$750 million for public liability). The risk of losses above these re insured levels is borne by the State.

Builders' warranty

On 13 March 2002, Victoria and New South Wales jointly announced a series of reforms to builders' warranty insurance arrangements. This announcement included a commitment to provide a catastrophe fund capable of supporting claims above \$10 million. To meet this commitment, the two states offered re-insurance arrangements to all builders' warranty insurers covering claims in respect of any one builder in excess of \$10 million, with each state reinsuring claims relating to properties in that state. South Australia has since also become involved in these arrangements. Since builders' warranty insurance commenced, there have been no losses by an insurer to any one builder exceeding this amount.

Victoria has re-insurance agreements giving effect to these arrangements with three insurers. The agreements require the insurers to pay the re-insurance premiums that are estimated to be sufficient for the states to at least break even on these arrangements. However, the State retains an unquantifiable contingent liability for additional claims.

Gambling licences

In 1992, a gaming operator's licence was issued to the Trustees of the Will and Estate of the late George Adams, now trading as Tatts Group. In 1994, the State issued a wagering and gaming licence to TABCORP Holdings Limited (TABCORP). These licences expire in 2012 and the end-of-licence arrangements are specified in the *Gambling Regulation Act 2003*.

These end of licence arrangements include compensation provisions for the licensees predicated on the current licensing arrangements being rolled over for a further period beyond 2012.

On 10 April 2008, the Government announced a new regulatory model for the post 2012 licences. Subject to legislative amendment, the main changes involve transitioning from the current gaming operator duopoly to a system where venue operators are licensed to own and operate gaming machines in their own right.

After considering the end of licence arrangements in the *Gambling Regulation Act 2003*, the government has formed the view that neither Tatts Group nor TABCORP will be entitled to compensation after the expiration of their current licences.

The Government does not intend to alter or amend the provisions in the *Gambling Regulation Act 2003* that deal specifically with the end of licence arrangements for Tatts Group and TABCORP.

