

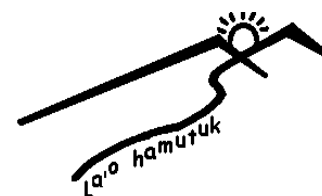
La'o Hamutuk

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15 November 2012

**to: Hon. Virgilio Maria Dias Marcal, President
and members of Committee C, RDTL National Parliament**

re: Opinion of the Court of Appeals on Timor-Leste General State Accounts for 2011

**cc: Other members of National Parliament, Court of Appeals, Minister of Finance,
media, website**

Dear Mr. President, with our respect,

Thank you for inviting La'o Hamutuk to participate in the Public Hearing today regarding the Court of Appeal's Opinion on the General State Accounts for 2011. La'o Hamutuk is grateful for the opportunity to share our thoughts with Timor-Leste's new Parliament, and we remain ready to help however we can in your challenging task of monitoring and authorizing the State Budget.

We also appreciate the hard work the Court of Appeals has done on a task which is the Constitutional responsibility of the High Administrative, Tax and Audit Court. The Court of Appeals has significantly increased its capacity since last year, producing a more comprehensive and insightful Opinion.

As the Court points out, the Government should have provided more information, and provided it on a timely basis. Fortunately, this Opinion is in time to inform Parliament's deliberations on the 2013 State Budget, which will be later than usual because of the formation of a new Government. We hope that next year's information on the 2012 State Accounts, including the Court's Opinion, will be available for Parliamentary discussion prior to the submission of the 2014 State Budget on 15 October 2013.

La'o Hamutuk has written several submissions and letters related to the 2011 State Budget and General State Accounts (GSA).¹ Last year, we suggested that the Court and Parliament should use more sources than the Treasurer's reports to help analyze the GSA, and we appreciate that the Court has also used the Deloitte reviews of procurement in 13 state agencies, although we share the court's disappointment with the Government's failure to provide come documents. We encourage both Parliament and the Court to utilize additional information, such from the Transparency Portals on budget execution and procurement, awarded contracts, ASYCUDA Customs reports, and other reports and analyses from state and independent experts. We suggest that the Court of Appeals be supported by an external auditor (other than Deloitte) in preparing its opinion, at least until the High Administrative, Tax and Audit Court is fully functioning.

¹ In addition to <http://www.laohamutuk.org/econ/OGE11/10OJE2011.htm>, we have written:

Topic	To whom	Date	Web link
2010 GSA	PN Committee C	28 Oct. 2011	http://www.laohamutuk.org/econ/OR10/TRaudit/LHtoComCGSA2010En.pdf
2011 State Budget	PN Committee C	15 Dec. 2010	http://www.laohamutuk.org/econ/OGE11/LHsubComCOGE11Dec10En.htm
2011 State Budget	President of Committee C	3 Jan. 2011	http://www.laohamutuk.org/econ/OGE11/LHtoCommC3Jan11en.pdf
2011 State Budget	President of the Republic	4 Feb. 2011	http://www.laohamutuk.org/econ/OGE11/LHtoJRH4Feb2011Te.pdf
2012 State Budget	PN Committee C	21 Oct. 2011	http://www.laohamutuk.org/econ/OGE12/LHsubComCPNOJE2012En.pdf

During Committee C's review of the 2010 GSA last year, La'o Hamutuk suggested that rapid budget growth is a symptom of the resource curse, and that repeatedly spending more than the Estimated Sustainable Income (ESI) from the Petroleum Fund for short-term convenience violates both the Petroleum Fund Law and good policy.² These points are even more important now.

In summary, we appreciate that the Court has made several reservations to its concluding Opinion that the state accounts are valid. Their recommendations, as well as others which Parliament may develop, should be made obligatory.

Unfortunately, as Deloitte's reviews of procurement practice show, enacting regulations without sanctions for breaking them is often ineffective. We encourage the Court and Parliament to report suspected legal violations to the Prosecutor-General and the Anti-Corruption Commission. When Parliament redrafts the proposed Anti-Corruption Law, we hope that you will include articles which compel compliance with procurement and other laws.

We would like to underline and expand on a few issues in the Court's Opinion:

- **We support all the Court's recommendations about accountability, timeliness, procurement practices** and more comprehensive and disaggregated information. These will not only facilitate the Court's review of next year's GSA, but will improve transparency and accountability to Parliament and the public.
- Last year, the Court recommended that **donor assistance** be included in this review and in the State's budget execution reports. This year, the Government and the Court have partially complied but information is lacking, due to incomplete data and mis-categorizing or repeating certain donors.³ Last year, La'o Hamutuk suggested that accounting for Timor-Leste's own funds is enough of a challenge, and we still believe that the Treasury and the Court should not try to include development partners in accounting of state finances.
- As the Court pointed out, **predictions of non-oil revenues** in the state budget are often wrong. A more detailed look, at each line of budgeted domestic revenues, shows larger discrepancies than the categorized totals. We suggest that the Ministry of Finance become more accurate at forecasting and efficient at collecting non-oil revenues, which will become increasingly important as petroleum wealth declines.
- In terms of **petroleum revenues**, the State Accounts and the Court's Opinion consider only the transfer of money from the Petroleum Fund (also a state entity) to the State Budget. We suggest that they should also include petroleum revenues (taxes, fees and royalties) received from the oil companies, as well as income and expenditures from investing the Petroleum Fund. Existing transparency rules and practices for the Fund should make this easy to implement. In 2011, petroleum dominated State finances, with oil and gas income comprising 97% of all State revenues.⁴ The Government is considering creating another sovereign wealth fund for mineral revenues, which underscores the need to regularize accounting for such funds.
- We agree with the Court's suggestion to include **revenues collected by all state agencies** in the GSA, including the National Petroleum Authority. In addition to those listed on page 11, the State Accounts should include finances of the Central Bank of Timor-Leste. The CGA and

² La'o Hamutuk letter to Committee C on the 2010 General State Accounts, <http://www.laohamutuk.org/econ/OR10/TRaudit/LHtoComCGSA2010En.pdf>

³ Note 7 to Consolidated Financial Statements incorrectly lists AusAID, European Union, JICA, CIDA, DGIZ, Monaco and KOICA.

⁴ According to the Ministry of Finance's 2011 Annual Report on the Petroleum Fund, oil and gas income was \$3,240.1 million and Petroleum Fund investment gross earnings were \$237.9 million. The CGA reports non-oil revenues of \$105.8 million.

Opinion should also discuss transfers from Ministries to other state entities, such as money appropriated to the State Secretariat for Natural Resources and then transferred to ANP and TimorGAP. If legal alterations are required to implement this accountability, Parliament should make the appropriate revisions to the law.

- We share the court's view that **Timor-Leste's infrastructure spending is overwhelmingly for electricity, to the detriment of other sectors.**⁵ We are also concerned that it is difficult to assess the value-for-money or good administration of state monies without information on the total costs of capital projects. The capital expenditures for the multi-year electricity project, which at over \$1 billion are more than triple what Parliament originally appropriated, should be a lesson which doesn't have to be learned again. ECTL's revenues will cover less than one-fourth of its operating costs (let alone the capital investment), which should be considered by Parliament and the Court.⁶
- 2011 was the first year of operation for Timor-Leste's new **Special Funds** – the Infrastructure Fund (IF) and the Human Capital Development Fund (HCDF), and they pose serious challenges to reporting and reviewing State Accounts. It is especially important for the Court and Committee C to look closely at these mechanisms to identify problems that need to be fixed, as with any new creation. We hope that this review will stimulate some revision of legislation and practices to make the Funds better serve the people of Timor-Leste, as significant weaknesses and gaps have become evident.

In particular, the problems around specifying and implementing the **MDG-Suco public housing program** should be addressed. The program was contracted for more than double the cost appropriated in the 2011 State Budget,⁷ but has not yet been paid. Prefabricated imports were justified on the basis of urgency, but very few of the houses have been built more than a year later. Questions have arisen about the social engineering motivations and value of the project, as well as its sustainability and whether the announced targets will be met.

Another disturbing item in the Infrastructure Fund spending, not mentioned in the 2011 State Budget, is the \$1,258,192 contract signed with Nevan Construction on 13 October 2011 to construct the official **residence of the Minister of Finance**, on top of \$283,515 signed in December 2010 with the same vendor for construction materials for the same home.⁸ When Parliament delegated budgetary reallocation power for the Infrastructure Fund to the Minister of Finance in Article 32.2 of Law No. 13/2009 of 21 October, you probably didn't intend it to be used in this way.

In addition, we reiterate our caution on the **Tasi Mane project**, which has already consumed nearly \$20 million of Timor-Leste's people's money for feasibility studies and preliminary designs. The total cost of this project will be many billions of dollars, and the return on investment is dubious. It would be better for Parliament to thoroughly examine this now, before a Final Investment Decision is made, rather than lamenting the lack of value-for-money ten years from now, after our petroleum wealth has been squandered.

⁵ La'o Hamutuk wrote about this at <http://laohamutuk.blogspot.com/2012/07/infrastructure-for-timor-lestes-people.html>

⁶ Fuel for ECTL accounted for four of the six largest contracts signed in 2011, totaling \$69.7 million.

⁷ The \$86.9 million contract signed with Carya Timor-Leste on 5 October was by far the largest contract signed during 2011.

⁸ Information from the Ministry of Finance Procurement portal on awarded contracts; this is the only residence for a Minister (other than the Prime Minister) among more than 500 contracts above \$249,000 listed between 2009 and 2012. See <http://www.eprocurement.gov.tl/publishedDocuments/show/10707> and <http://www.eprocurement.gov.tl/publishedDocuments/show/6335>.

Unfortunately, some important issues were not discussed in the Court's Opinion.

- **Contingency Fund** – Although the Appeals Court Opinion says that the GSA 2011 complies with the Budget and Financial Management Law, we have a different opinion. Article 37 of this Law states that contingency funds can be used for “urgent and unforeseen expenses,” and in 2011 Timor-Leste spent \$29.5 million from contingency money, just below the 5% legal maximum.

The \$176,322 in contingency funds spent to pay the salary of Finance Ministry advisor Olgário de Castro during 2011 could have been anticipated before the budget was approved. At the same time, Olgário de Castro was President of the Investment Advisory Board for the Petroleum Fund. We wonder why he should receive a special urgent salary, rather than being paid out of the Ministry's appropriation for consultants.

In addition, the Ministry of Defense and Security spent \$1.6 million in contingency funds to continue construction of the Hera naval port and \$2.8 million for roads and drainage for the integrated border posts. The Ministry of Education spent \$4 million from contingency funds for nearly a hundred items, including international travel and salaries for consultants and UNTL professors (both national and international). Timor-Leste spent \$174,300 for scholarships to APTECH-India (where our students were unable to study), \$170,000 for an advertisement in Foreign Policy Magazine, and nearly \$10 million on fuel. We believe that these and many other contingency fund expenditures were predictable or unwise and should have come from normal ministerial budget allocations or not have been done. This pattern undermined Parliamentary authority, encourages poor planning, and weakens state transparency and accountability.

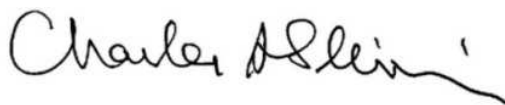
- **The state spent more money on fuel than the total value of fuel imported.** The 2011 State Accounts show that State agencies spent \$67.7 million on fuel for vehicles and generators, but the DNE's 2011 External Trade Statistics report shows that the total value of diesel and gasoline fuel imported was only \$38.6 million for all state, commercial and private users. We wonder if something is wrong with this process, and we suggest that Parliament could ask Government to explain this discrepancy to ensure that money is being spent as it should be.
- We are also concerned that state expenditures during 2011 gave **low priority to human resources and social development, local economy and rural infrastructure**. 90% of the money spent from the Infrastructure Fund went to the electricity mega-project – while hardly anything was allocated to rural roads, water and sanitation. Timor-Leste spent about one-third as much of its state budget on health and education as other developing countries, which betrays our families and our future.

Thank you very much for your attention, and we look forward to continuing this collaboration.

Sincerely,



Juvinal Dias



Charles Scheiner



Tonilia dos Santos

Researchers, Natural Resource and Economy Team, La'ó Hamutuk