Unofficial rough translation by La'o Hamutuk.

VIII CONSTITUTIONAL GOVERNMENT

Proposed Law Approving the State Budget for 2018

Statement of reasons

Introduction

Pursuant to Article 97.1(c) and Article 115.2(a) of the Constitution of the Democratic Republic of Timor-Leste, the Government proposes to the National Parliament the present Proposal of the General State Budget (OGE) for 2018.

The present Proposed law for OGE 2018 covers all income and expenditure of the State and Social Security of Timor-Leste and covers the period from 1 January to 31 December 2018.

Grounds for the proposal

The VIII Constitutional Government Program, recently approved by the representatives of the Nation, seeks to respond to the new and increased challenges of the current development stage of our country and to guarantee the improvement of living conditions and the raising of the welfare level of the Timorese people, on the path to the realization of the Strategic Development Plan 2011-2030 and the Sustainable Development Goals.

In our specific conditions, the state's responsibility in promoting development is increased, because it is its responsibility to create basic economic and social infrastructure, invest in human capital and provide an institutional framework conducive to the diversification and growth of the economy.

The pursuit of these objectives requires the implementation of appropriate policies with a high level of effectiveness and efficiency, and for this a condition that the objectives of governance find full translation in the allocation of resources and in the Budget of the State, in a general manner.

This is, however, a budget that is adopted at a time when much of the financial year is already past. The law establishes that the budget execution processed in a duodecimal regime, conditioned by legal and procedural restrictions, is integrated into this year's State Budget, which therefore reflects this reality.

Thus, the State Budget proposal includes appropriations for the budget execution processed in twelfths which was based on the State Budget for 2017 adapted to the governmental structure, in the light of the rules on twelfths, in article 31 of the Law on Budget and Financial Management. The table below details budgetary expenditures for the current fiscal year by disaggregating information on the temporary budget appropriations executed between January and June 2018 and for July and August 2018 and budget appropriations to be carried out between September and December 2018.

($ millions)	OGE 2018	Actual DOT 2018 Jan - Jun	DOT 2018 estimate Jul - Aug.	OJE 2018 Set - Dec.
Total expenses	**1.218.0**	**402.1**	**100.4**	**715.5**
Recurrent	883.9	301.0	82.7	500.2
Wages and Salaries	200.3	89.1	29.7	81.5
Goods and services	397.8	119.4	29.9	248.5
Public Transfers	261.9	87.7	21.9	152.3
FDCH	23.9	4.8	1.2	17.9
Capital	334.1	101.1	17.8	215.3
Minor Capital	3.7	0.0	0.0	3.7
Capital Development (ex-loans)	330.4	101.1	17.8	211.6

In addition, responsibilities and commitments have been accumulated for civil servants, suppliers and partners, imposing burdens and non-discounting costs. This budget aims to put an end to this situation, almost entirely, creating better conditions for the state to fully perform its functions.

In view of these circumstances, the adoption of this Budget proposal is of the utmost importance and, for it, a request for priority and urgency in the assessment of the budget is justified**,** since the present proposal reinstates normality in budgetary implementation, allowing priority needs to assist the recovery of economic growth, to provide conditions for the installation of the VIII Constitutional Government and, at the same time**,** to lay the foundations for the implementation of the governance program.

Petroleum Revenues

In preparing the state budget for 2018 the petroleum wealth was estimated at $18,345.8 million. Therefore, Estimated Sustainable Income (ESI) of 3% is estimated at $550.4 million. This amount is higher by $75.3 million than the estimate for 2018 in the budget of the previous year.

Petroleum revenues for 2018 are estimated at $317.1 million, considering the actual receipts and the price of oil from January to June and the futures price for the second half of the year. The ROI is 1.7%, which translates into an investment return of $282.8 million.

It is expected that the balance of the Fund will be $16,414.4 million at the end of 2018 following the withdrawal of $984.8 million in 2018 to be approved by the National Parliament. The estimated withdrawal is $434.4 million higher than the ESI for 2018.

The Petroleum Fund's investment policy is based on an asset allocation and risk limits as defined in the Petroleum Fund Law as revised in August 2011. At present it is applied to 40% in stocks and 60% in bonds of public debt. The investment strategy was designed to target a real return of 3%, which would compensate for the withdrawal of ESI and preserve the Fund's purchasing power.

The Human Capital Development Fund

The Government, in 2011, regulated, through Decree-Law no. 12/2011, of March 23, the Human Capital Development Fund, established pursuant to article 32 of Law no. 13/2009, of 21 October, on Budget and Financial Management, and article 9 of Law no. 1/2011, of February 14, which approved the OGE for 2011.

This instrument will allow the Government to continue investing in the training of its people, since the technical and academic qualification of human resources is the key to success of any country that wishes to be modern and creative in the future.

Non-Petroleum Revenues

The good performance of domestic revenue in 2016 deteriorated to $189.5 million in 2017. This means a reduction of 5% compared to the effective collection of 2016 and resulted from the unfavorable macroeconomic conditions that prevailed in Timor-Leste in 2017.

The reduction was mainly driven by reduced tax revenues, which are more sensitive to GDP fluctuations and make up the bulk of domestic revenues, as rates, licenses and tariffs have grown.

A steady evolution is expected in 2018, with a projected collection of $188.8 million. The lack of improvement in total domestic revenue reflects the prolonged climate of uncertainty for much of 2018.

Domestic revenues are only a small part of overall revenues and therefore do not fully compensate for changes in oil prices and return on investment. This underlines the importance that should be assigned in the future to increasing domestic revenue streams.

Public debt

Article 20 of Law 13/2009, of 21 October, on Budget and Financial Management, as well as Law no. 13/2011, of 21 February, on the Public Debt Regime, provide for the possibility of borrowing by the State.

It is with this legal basis that the Government submits to the National Parliament a proposal for authorization for the contracting of additional concessional loans up to $44 million for a maximum term of 40 years, as well as mobilization and disbursements up to $61.6 million, which by legal obligation should be used only for the construction of strategic infrastructures for the country's development.

Expenditures entered in the State Budget for 2018

Wages and Salaries

The total budget for wages and salaries is $200.312 million. This amount is decreased by 4.5% in the 2018 State Budget compared to the appropriation for 2017. This is motivated by the fact that many ministries and agencies have budgeted in excess for this category in 2017, in the expectation of recruiting more staff throughout the year. For several reasons, this new hiring did not materialize. As such, budgets have been adjusted to more accurately reflect current needs and commitments with existing public servants in 2018.

Goods and services

The total budget for the Goods and Services category is $421.666 million, which represents an increase of 8.1% compared to the allocation in the State Budget for 2017. This increase is due to the payment of obligations and outstanding commitments provided in previous years which have not been paid in full.

The main measures in this category include, but are not limited to:

- $82. million for fuel and maintenance of electricity generators in Hera and Betano;
- $22.4 million allocated in appropriations to Whole of Government for the Contingency Reserve;
- $18.1 million for legal services;
- $18 million for payments related to national elections;
- $14.4 million are allocated to municipalities for the program and the school feeding program, subsidies for schools and operating costs and services for administrative authorities;
- $10.3 million to SAMES for drug procurement and improve the quality of health services across the country;
- $4.8 million for a clean water and sanitation program in rural and urban areas.

Public Transfers

The total budgeted for category Public Transfers is $261.925 million, which represents a reduction of 37.8% compared to the State Budget for 2017. This reduction is driven by a decrease in the budget allocated to the Special Administrative Region of Oecusse Ambeno (ARAEOA) and the Special Economic Zones of the Market Economy of Oecusse Ambeno and Atauro (ZEESM).

The main measures in this category are:

- $98.9 million for pensions and broader support to veterans. This program includes support for the most vulnerable.
- $48.1 million for social programs, including old-age pensions and disability, and survivors (including social pensions / allowances for the Elderly and Disabled and pensions under the transitional social security scheme), Bolsa de Mae, and support for victims of natural disasters;
- $28 million for the Special Administrative Region of Oecusse Ambeno (ARAEOA) and the Special Economic Zones of the Market Economy of Oecusse Ambeno and Atauro (ZEESM);
- $13.7 million for the Contributory Social Security System;
- $12.4 million for medical treatment abroad;
- $12.1 million to support the National Petroleum and Minerals Authority (ANPM), TIMOR GAP and the Petroleum and Geology Institute (IPG) ;
- $7.5 million for the municipalities to support urban cleaning activities, school feeding programs and scholarships, and contribute to rural development and inclusive growth;
- $6.5 million to support the Bishops' Conference of Timor-Leste.

Minor Capital

The total budget for this category is $3.659 million which represents a reduction of 69.7% in relation to the State Budget for 2017. This reduction is justified on the ground that the expenses for Capital Minor were frozen during the part of the financial year covered by the duodecimal system.

The main measures in this category include, but are not limited to:

- $1.3 million for computer equipment, furniture and other start-up costs needed to support the new Government structure;
- $0.7 million to buy hardware and equipment to update and improve the informatics system for financial management;

- $0.5 million to acquire furniture for the houses for Veterans in Los Palos and equipment for the dormitories at Hera Polytechnic;
- $0.3 million to buy a new electricity transformer.

Development Capital

The total budget for the Development Capital category is $392,037, including loans for this category in 2018 totaling $61.6 million which are allocated to the Infrastructure Fund.

The budget for this category, excluding loans, has increased by 33.7% compared to the allocation for 2017. This is driven by an increase of 45.4% in the budget for the Infrastructure Fund, to meet the financial needs of projects in progress.

The Development Capital budget under the Treasury Account is divided into $323.6 million for the Infrastructure Fund, $3.1 million for PDIM and $3.7 million for other capital project development allocated to ministries.

New policy measures:

The Government proposes to resolve the debts and contractual obligations accumulated in recent years, which have not yet been paid. The total cost of such payments is $87 million, broken down as follows:

- $64.5 million allocated to Whole of Government Appropriations to reimburse KITAN exploitation taxes;
- $6.9 million for retroactive payment of salary increases for teachers in seven municipalities who received promotions between 2013 and 2017;
- $5.8 million allocated to fast customs clearance;
- $4.5 million for payment of debts to Timor Telecom;
- $2.2 million to pay off electricity bills;
- $1.5 million to the National University of Timor Lorosa'e to pay off the various debts accumulated between 2016 and 2017;
- $0.8 million to the National Police of Timor-Leste to cover debts relating to the maintenance of vessels, CCTV and telecommunications;
- $0.5 million for the FALINTIL - Timor-Leste Defense Force, to pay several outstanding subsidies and additional costs associated with the recent elections;
- $0.3 million to cover the remaining unpaid costs of the 2016 suco elections.

Social Security

Through Law no. 12/2016, of November 14, the National Parliament approved the creation of a social security contribution scheme, which is characterized by being a single system for all, integrating the beneficiaries of the mandatory, self-financed, transitional system with financial independence in relation to the State Budget.

The Social Security Budget (OSS), which has a range of control and approval mechanisms similar to those seen in the State Budget, is assessed and approved separately in annual cycles as the central control and monitoring instrument evolution and planning of the system by the organs of sovereignty.

In 2018, however, it is opted to include in the scope of the Social Security Budget only the budget of the contributory social security scheme in its distribution and capitalization components (Social Security Reserve Fund), excluding the subcomponent of the transitional social security scheme. Also, the Social Security Administration budget and the non-contributory social security budget are not included in the OSS scope in 2018. This is due to the fact that the National Social Security Institute is not yet in full operation and it is considered more correct and more practical for OSS to integrate the budgets of all its components/regimens only when that Institute finds itself in full operation, with effects only, predictably, in the OSS for 2019.

Global Social Security Revenues amount to $41,149,945, of which $24,833,390 are effective income for the year 2018 (including $24,831,890 of contributions to social security) and $16,316,555 are balance carried over from the previous year.

Complying with the rule of budget balance, the total of the Global Social Security Expenses is also $41,149,945, of which $716,541 are effective expenditure of the year 2018 (including $713,041 in current transfers for the payment of benefits to beneficiaries) and $40,433,404 are expenses on financial assets, referring to investments of the accumulated amount in the Social Security Reserve Fund.

Among the estimates of actual revenues and expenditures of the OSS for the year 2018 there is therefore a foreseeable accounting balance of $24,116,849 (= $24,833,390 of actual revenues of the year 2018 - $716,541 of actual expenditure of the year 2018), relative to the account balance of the Contribution Regime of Social Security - Distribution Component, which will be transferred, until the end of 2018, to the Social Security Reserve Fund, in compliance with the law. Likewise, also the amount of the balance carried over from 2017 will revert to the Social Security Reserve Fund.

It is thus expected that the total of 40 accumulated in the Social Security Reserve Fund will be $40,433,404 (= 24,116,849 related to the balance generated in 2018 and $16,316,555 relating to the balance carried forward from 2017 and not yet transferred to the Fund), transferred from the Security Contribution Regime Social - Distribution Component, and that this amount be applied, in order to capitalize income.

The partial tables of receipts (Tables II and III of Annex II) and the expenditure (Tables V and VI of Annex II) of social security schemes, which form part of the OSS budgetary scope for 2018, are not, of course, the same as the consolidated totals (Table I of Annex II) and expenditure (Table IV of Annex II) of the OSS for 2018, since, in the latter, transfers between social security schemes (from the capitalization component), in the aggregate value of $40,433,404.

Approved by the Council of Ministers on 2 August 2018.

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