NATIONAL
PARLIAMENT
Democratic Republic of Timor-Leste

Public Finance Committee

Report and Opinion
based on initial assessment of Proposed Law No. 1/III
First Amendment to Law No. 16/2011 of December 21, approving the State Budget for 2012

October 9, 2012

INDEX

ANNEXES

1. INTRODUCTION

1.1 Admission

The Draft Law (PPL) no. 1/III - First Amendment to Law no. ° 16/2011 of 21 December, approving the State Budget for 2012 was presented by the Government on 14 September 2012 in terms provided in Article 95.3(d) and (e), Article 97.1(c) and the n. 1 of Article 145.1, all of the Constitution and also in Articles 162 and following the Rules of Procedure of the National Parliament (Rules).

Since that proposal was announced in plenary and admitted on the same day, by order of His Excellency the President of the National Parliament, was given its distribution and handed down to the Committee on Public Finance, for the Report and Opinion, and to the other specialized parliamentary committees to issue their sectoral opinions.

1.2 Issue Preview and appointment of rapporteur

The Committee on Public Finance considers that it has jurisdiction in the matter, to enjoy the legislative initiative allowed in formal terms and in relation to its content material.

Rapporteurs were designated the Excellencies Adozinda Pires da Silva of Frente Mudança (FM) Parliamentary Caucus , and Maria Fernanda Lay, the Parliamentary Caucus of the National Congress of Timorese Reconstruction (CNRT).

In preparing this Report we observed, mutatis mutandis, the provisions of Article 34 of the Rules of Procedure.

1.3 Public Hearings

Under the rules, public hearings were held between 21 September and 2 October 2012, which heard the following entities:

- The Government, in the persons of Excellencies Ministers of Finance, State and the Presidency of the Council of Ministers, Public Works, Trade and Industry, and Petroleum and Natural Resources and Excellencies Secretaries of State for Trade and for the Support and Promotion of the Private Sector;
- The Central Bank of Timor-Leste, which was represented by a delegation for this purpose mandated by the Hon. Governor;
- The National Development Agency;
- The National Procurement Commission ;
- The Major Project Secretariat.

During the public hearings, the Government presented the proposed law to the Committee and the above entities had the opportunity to express their views and to inform MPs about their position in relation to the proposed budget that is now being discussed.

2. LEGAL FRAMEWORK

Under the constitution, Parliament is responsible, in addition to the primary functions of representation and legislative activity, to monitor and supervise the executive and hold the Government accountable.

This feature translates into a parliamentary power - duty to assist Members and has, since then, essentially political, but is particularly relevant in relation to the use of public financial resources, constituting a privileged instrument to ensure greater transparency and public scrutiny of political activity - administrative and good governance.

Under conjunction with Articles 115.1(d) and 145.1 of the Constitution, the proposed State Budget is the sole initiative of the Government and shall be submitted to the National Parliament, under the form of the bill, by 15 October each year.

In terms of substantive law, the budget system, and framed by the Constitution, is also governed by Law No 13/2009 of 21 October - Budget and Financial Management.

Article 34 of Law No 13/2009 of 21 October - *the Government may propose amendments to the state budget in effect when the circumstances so warrant* -- applies here, there having been a change in the governmental structure with the approval of the Organic Law of the V Constitutional Government, following the legislative elections last July and the beginning of the Third Legislature of the National Parliament.

Appreciating Proposed Public Law (PPL) 1/III in the light of formal requirements that must be satisfied for its admissibility, it appears that complies with the provisions of Article 92, 96.2, 98 and 162 of the Rules, considering that it is written in Portuguese language, in the form of articles, contains a title which reflects its core purpose and is accompanied by explanatory memorandum being submitted in accordance with the provisions of Article 34 cited above of Law no. 13/2009 of 21 October.

With regard to its external configuration, such as steel or normative instrument, the bill under consideration obeys, in general, the essential rules of formal legislation, suggesting only a reformulation, based on specialty, the text of Articles 1.1 and 1.2, in order to give greater clarity, explaining its entire line with the legal and procedural requirements and in particular those arising from Article 34.2 of Law no. 13/2009, October 21 and Article 167 of the Rules of Procedure.

The Committee, therefore, finds that it meets the formal requirements for submission of bills, as provided by law and the Rules.

With regard to organic requirements, it is exclusive parliamentary legislative competence pursuant to subparagraph Article 95.2(q) and Article 145.1 of the Constitution, that Parliament is the appropriate body to decide.

Regarding the normative content, it appears that, under the proposal, and according to the information available, there are no changes in the amount of transfer from the Petroleum Fund or the Public Debt, against the ongoing State Budget, approved by Law No 16/2011 of 21 December.

So, legally, against the applicable legal framework, we see nothing that would impede consideration and possible adoption by the Parliament of the proposed side, under terms of Articles 166 and those after it and the Rules of Procedure.

3. MACROECONOMIC FRAMEWORK

Development of the Global Economy

It remains the scene of stagnation in the major economies (*developed economies*), it is observed despite some signs of recovery in employment in the U.S. economy. In this framework, the stronger European economies are struggling even with the effects of the recession affecting its major trading partners on the continent.

The scale of the recession in the Eurozone not only affects the growth rate of other world economies, but also generates some disorders in countries that in the past two years seemed immune to such effects. In Southeast Asia, is becoming increasingly evident slowdown in many economies, very similar to what happens in the larger Latin American countries such as Brazil and Mexico.

The strategies adopted by *domestic orientation* of most emerging economies (such as for example Malaysia, Thailand, Indonesia and Brazil, etc.) over the past five years, since the onset of the global financial crisis, it worked relatively well, but the moment begins to reveal some signs of fatigue.

Despite the expansionary policies that have been implemented in these economies, some inflationary pressure led to a significant appreciation of their currencies against the U.S. dollar and the Euro, reducing their competitiveness in the short term, while on the other hand devaluation of the Euro has suffered in relation to the rest of the world, further amplifying the effects of appreciation of the currencies of these economies.

Prices of tradable goods

A minor speculation on tradable goods, in terms of quantities traded, determined a greater price stability with regard to food and to a lesser extent, to mineral products.

The impact of the recession and reduced growth expectations for China and India, had the effect of lowering prices of materials - highly dependent on the levels of production and industrial activity in the construction sector - to values lower than anticipated in early 2012.

For agricultural products or food and, especially in the case of seeds and grains, reduced precipitation (dry) in the United States and Russia came to result in a positive change of price behavior, which is only now beginning to stabilize, after the highs reached in 2006-2008, when prices peaked.

Oil prices remained near $100 during most of the year as a result of instability in the Middle East and the lack of agricultural surpluses for the production of biodiesel. Nothing indicates that this trend will reverse in the short term, so it would maintain a stable level of income from petroleum to Timor-Leste. Nevertheless, there were variations over 2012, with the oil price increase earlier this year, that trend was reversed between May to August, when it began to rise again.

The forecasts for the first part of the year are ambiguous. If the global recession continues, prices will fall, but the instability in the Middle East and the lack of surplus production of grains and cereals, limited to replacement by biodiesel, impacting on high oil prices. The most likely scenario is similar to what has been observed throughout the year, with oil prices hovering around in the $95-$100 per barrel, with great volatility within the range, which is not a negative outlook for the resources of the country. Anyway, this will only serve to offset the price of food that the country imports large scale to meet the needs of the population.

It should be noted that the predictions for 2012 were initially very optimistic, after having been revised downward in most cases. If the solution in the Eurozone continue to go through the traditional framework of austerity, optimism for 2013 should be moderate. The same happens if changes occur in the U.S. administration and the cuts announced by the opposition during the campaign are carried out.

National economic framework

The economy of Timor-Leste relies heavily on state expenditure to ensure a reasonable growth rate and the year 2012 was not an exception. The weight of public spending is nearly double the non-oil GDP, which is relevant situation, especially when much of the non-oil economy is used for self-consumption, reducing the surplus that can be traded in the market.

The need to understand domestic economic activity and the role of the private sector, is crucial to implement measures that help to more balanced growth throughout the country, as well as to avoid decisions that may lead to conflict which are difficult to resolve. This will also help analyze other issues that are crucial to the state budget, such as inflation.

The private sector in Timor-Leste

The National Directorate of Statistics published in 2010, the “Business Activity Survey” (BAS), in which it provides a *snapshot* of the real and deep structure of the private sector in Timor-Leste. The BAS shows that the private sector is concentrated in the area of Dili, where 91% of sales, corresponding to about $900 dollars for 2010. Considering the available data, it seems to conclude that this level of activity will be kept for the period between 2011 and 2012.

Moreover, considering the total employment, is clearly a distortion in its distribution, since 83% of the employed population works in Dili. These numbers reinforce the concern about the imbalance in the growth of the country, reinforced this concern in relation to other indicators: 92% of purchases of materials, supplies and finished goods are done in Dili ($390 million, totaling $423 million).

The above trend also affects workers' wages. The annual average wage of workers in Dili is about $2,100, while the districts only reaches $900 (BAS, 2010). In principle, although the data are not very clear, the same trend applies to the government and public employment, increasing this effect.

Such issues should be considered with a more integrated approach, giving attention to the experiences of rapid growth of urban centers, not only in Southeast Asia but also in the Pacific, which had a negative effect on the welfare of populations, costs production in the private sector and additionally in providing social goods and services by the state, making inefficient and ineffective interventions through public policies.

Moreover, the embryonic development of the private sector reveals a figure compatible with the structure of oligopoly. The profits in the region of Dili represent on average 25% of total sales, while labor costs represent only 10%. In the districts, the ratio is 41% for profits and 9% for total labor cost. The ratio between revenue and capital expenditure reflects those values dramatically.

The process of capital accumulation in the private sector in the country is very clear. The policy of expansion of the state through investment in capital goods, especially infrastructure, is essential for the country in its transition to a more open market economy. The size and weight of the private sector is still limited to the production of consumer goods and services, and commercial activities account for one third of total sales. Construction (10%) and manufacturing (6%), traditional sectors in the production of goods, are still residual activities in Timor-Leste.

Capital accumulation

The process of capital accumulation is essential for the economic development of the country, not just for the private sector, but also for the acquisition of infrastructure and productive services from the state, which can be used by companies to increase their potential productive and economic competitiveness. The state has sought to meet the challenge, but so often disconnected from economic reality we ignore the other factors relevant to development that is more than mere growth (economic).

Inflation

Inflation is an important aspect to consider while preparing the state budgets, especially in a country where the state has a significant influence on overall economic activity. In fact, inflation directly affects government revenues throughout the year, while it affects their spending in a country like Timor-Leste, where there is no monetary sovereignty, that is, in a country that does not issue its own currency and depends on external sources.

The way inflation is interpreted or understood also defines public policies that affect not only public finances, as well as the general population, especially those on fixed incomes, who have no defense or protection against inflation.

When analyzing inflation, we should take into account three factors: those which put pressure on inflation, those which propagate inflation and those which validate inflation. If this is not clear, wrong interventions can have dramatic effects not only in the accounts of the public sector, but also in the *wallets* of citizens.

In the case of Timor-Leste, the factors leading to the rise in inflation are the prices of imported goods. The appreciation of the value of the currency of RDTL's major trading partners against the U.S. dollar, in addition to the high level of food prices, accelerating the growth of annual inflation above 10%.

The external influence on the price increase is spread and propagated by trade oligopoly structures that transfer increases in prices, without affecting the high level of profits that can be seen from reading the BAS, mentioned above.

Validation of inflation is defined by liquidity (*cash payment*) that is held by the population that buys goods and services, despite rising prices. In this context, what should be the solution? It will certainly not be easy. Increasing external competitiveness at any cost can seriously affect business, some of which remain in the country for a long time. Reducing government spending could have a negative effect on disposable income in some sectors of the population and fiscal spending multiplier effects, in most economical activities.

The recommendation will be more sensitive and rational to increase the efficiency and effectiveness of public expenditure, reducing and avoiding the tendency to spend on goods and services in a consumerist way, mostly on imported goods and services.

The second recommendation is to try to reduce the constraints that limit domestic supply of essential goods, adding to their cost of production.

Some of these constraints relate to the conditions of transport and the cost of the market, but the most significant are, in a country with a high level of rural production, prices of consumer goods for the rural population.

Considering inflation in this country from an *urban perspective* or with the *eyes of the urban sector* is not entirely appropriate. Without a thorough understanding of what is the phenomenon of inflation in the context of a pre-capitalist economy, it is very likely that some incorrect measures are taken, dramatically affecting the quality of life of the most vulnerable sectors of the population who depend mainly on prices of fuel and food commodities such as rice, for their livelihood.

4. OBJECTIVES OF ECONOMIC AND FISCAL POLICY

The recent parliamentary elections, held on 7th July, produced changes in the political forces in power, and the V Constitutional Government supported by a coalition of three political parties, the National Council for Timorese Reconstruction (CNRT), the Democratic Party (PD) and Frente Mudança (MF).

This change of political forces had some impact, as would be expected, on the economic and financial objectives set by the previous government in 2012, as reflected in the new structure of the government and the corresponding adjustments to appropriations for the General State Budget for 2012, previously approved by the National Parliament.

In the *Rectification Budget Book* accompanying the bill submitted on September 14, 2012, the Government says *it is determined to maintain strong economic growth, improve service delivery and reduce poverty.* To achieve these objectives, the Government created a new organizational structure, which includes six new ministries, namely the State Ministry for the Presidency of the Council of Ministers, Ministry of Commerce, Industry and Environment, Ministry of Public Works, Ministry of Transport and Communications, Ministry of Petroleum and Mineral Resources and the Ministry of Tourism and the extinction of some others, in addition to creating new Secretaries of State, the Secretary of State for Parliamentary Affairs, the Secretary of State to Support the Promotion of the Private Sector, the State Secretariat for Strengthening Institutional and State Secretariat for Social Communication.

As has been said in the book mentioned above, *the new ministerial structure and the transfer of responsibilities between ministries will facilitate better coordination of the formulation and implementation of policies.*

A new governmental structure and its economic and financial objectives have translated from the budget under the bill now being discussed, as well as in the respective tables.

The Rectification Budget does not include any changes in fiscal policy for the current financial year, the Government keeping unchanged the estimates of oil and non-oil revenues contained in the State Budget for 2012, as well as the level of public debt.

It appears that in the proposed Rectification for 2012, similar to what happened with the proposed State Budget for 2012, the Government has decided not to set sufficiently explicit concrete and measurable goals to reduce absolute poverty (poverty line) and relative poverty (income distribution), linking them as the only options for fiscal policy proposals.

Thus, some of the key issues that should be clarified in the general debate on Proposed Law 1/III relate to the direct impact that, in the Government's perspective, the state budget will have on poverty reduction and unemployment and growth strategies for the non-oil economy.

The question of controlling inflation, unsustainable in the medium term in Timor-Leste, if it remains at current level, also takes on special importance, this shifts resources from where they are most needed. Inflation, as the Central Bank underlined before this Committee in the public hearing, is more of a "hidden tax" because it reduces the purchasing power of the population having a particular impact in Timor-Leste, where wages in average terms, are quite small, so measures to control inflation seem indispensable.

Moreover, it appears that, although the Government announces its intention of promoting human resources development, budgetary translation of this option is very residual in the State Budget for 2012, as it only gives an overall allocation of $30 million to the Human Capital Development Fund (HCDF), corresponding to 1.8% of the overall expenditure earmarked for 2012.

That allocation remains relatively low in the proposed Rectification budget for 2012, the Government opted to keep unchanged the forecast of HCDF initial expense, while increasing spending in the state budget by more than $124.9 million with this rectification budget proposal. It can therefore be questioned whether the accounts presented by the Government to the National Parliament, do not adequately reflect this growth in public spending.

On the other hand, one cannot fail to notice the little or no execution of some of the projects in HCDF (see, e.g., Budget Execution Report until 8 August 2012, p. 2-3 of Map of Execution the HCDF), since the qualification of human resources in strategic knowledge areas, particularly in the field of agriculture, is of utmost importance for the country, as has been unanimously recognized.

On the other hand, there is the commitment of the Government in the development of basic infrastructure like electricity network, sanitation, water supply and construction of roads, bridges and ports, but it is important to reflect upon the medium term return of these investments and the trend towards rapid depletion of oil resources, that is, about the sustainability of current government strategy.

One cannot fail to be alert to the fact that high dependence on imports of most goods and services related to building infrastructure leave the economy relatively weak, further contributing to the increase in domestic inflation. From the perspective of long-term sustainability and intergenerational equity, we believe it is necessary to refocus priorities of development, with a view to more efficient management, gradual and phasing out oil resources.

5. STRUCTURE OF THE STATE BUDGET RECTIFICATION FOR 2012

PUBLIC REVENUES

The table below shows the sources of **funding for the State Budget for 2012** and the appropriations therein. It shows that 90% of expected revenues in the budget come from the Petroleum Fund ($1,495 million).

Table 1 - Financing the State Budget 2012

(Million USD)

Sources of Funding	2012	% of GSB
Domestic revenues	136.1	8.1%
Estimated Sustainable Income (ESI)	665.3	39.7%
Transfers above the ESI	829.6	49.6%
Use of Cash Balance	0.0	0.00%
Borrowing	43.1	2.6%
TOTAL	**1,647.1**	**100%**

The draft rectification budget introduces changes in the composition and amounts of revenue that will bear additional expenses to be paid in 2012, thanks to reinforcement of $124.9 million in revenue component, through the integration of all Infrastructure Fund balances carried over from 2011.

Table II-Funding Rectification State Budget for 2012

(Million USD)

Sources of Funding	2012	% of GSB
Domestic revenues	136.1	7.6%
Estimated Sustainable Income (ESI)	665.3	37.0%
Transfers above the ESI	829.6	46.1%
Use of Cash Balance (Infrastructure Fund)	124.9	6.9%
Borrowing	43.1	2.4%
TOTAL	**1,799.00**	**100%**

The increased allocation in the Infrastructure Fund of $124.9 million, reveals inaccuracies in information contained in the Draft Rectification Budget Law for 2012, stating that "the total expenditure of the state budget remains unchanged, at $1,674.1 billion," when there is an increase in overall revenue for 2012 recorded at $124.9 million, from the balance carried forward from the Infrastructure Fund at the end of 2011, and naturally, a reinforcement of equal value in budget spending, as indeed provides the balanced budget rule.

Another inconsistency is detected in relation to compliance with the budgetary principle of unity and universality that, under Article 4 of the Law on Budget and Financial Management, states that "the State Budget is only one and includes all expenses and revenue for state services without financial and administrative autonomy and autonomous services and funds," that because the Government carries out the integration of 2011balances carried forward from the Special Funds, but not the balance of the Human Capital Development Fund. It is understood that the Government should take this opportunity to integrate all balances carried forward in this first budget amendment, thereby ensuring the availability of all relevant information to Parliament, which by law must dispense. The Budget Execution Report to August 8, 2012, shows a value of $7.45 million for the balance carried over from the Human Capital Development Fund, which the government promptly clarifies that it reserves the right to later add the amount unspent in 2012.

We also notice some difficulties in raising additional revenue even in 2012, perhaps due to, among other factors, insufficient supervision of economic activities, and the government should take steps to ensure, for example, that the accounting firms effectively reflect their billing.

Also point out the unreliability of some data provided by the Government on the execution chart of the **Human Capital Development Fund** at August 8, 2012, which includes balances carried forward from 2011, by negative values for some of the projects, which according to the balanced budget rule would not be allowed, since the payments made on account of any item of expenditure can never be higher than the budget approved and registered.

On the other hand, it is in compliance the allocation of Combined Sources Budget will now be set by the Government, from the initial $188.9 to $221.8 million, the contribution of **Development Partners** to the State Budget of 2012 , this contribution gives priority to the institutional strengthening of the public sector, infrastructure, education, health and agriculture. Despite the Government inform that there is an Aid Management Platform (PGA/AMP), stating that it contains all available information about foreign assistance, based on discussion of rectification budget for 2012, should submit to the National Parliament their detailed execution, by sector.

The contributions of the **Petroleum Fund** to the State General Budget for 2012 Remain unchanged with the amended budget, totaling $1,494.9 billion, 665.3 million of which corresponds to the Estimated Sustainable Income (ESI) for 2012 and $829.6 million increased financing needs above the ESI for the year under review. However, the transfer of an additional amount as meaningful again deserves some repairs, at the outset by the fact that it has the power to compromise a Fund that is vital to the economic and financial sustainability of the country in the long term and thus, ultimately, could come to mortgaging the future of generations to come.

CURRENT EXPENSES

The *Rectification Budget Book for 2012* presents, on page 6, a table with additional expenses to be included in the Rectification Budget for 2012, which is reproduced below in Table III. It underlines the lack of rigor in some calculations, which detects to make the calculation of total expenses. Indeed, the sum of additions by the Government introduced additional expenses totaling $50.1 million and not $50 million as registered. This is a remarkable deviation of $100,000 , which it is the government justified during the debate on the draft rectification budget.

Another situation that requires further explanation from the Government relates to what may result from the reading of that same table on page 6, where only informs Parliament about "additional expenses of over $1 million" as the title refers. You can then withdraw that no additional information on costs of less than $1 million? Ultimately, the sum of all unreported costs up to $ 1 million, could amount to millions of dollars.

Regarding the additional expenditure proposed in the Rectification Budget, on the other hand there is to report the transfer of $50 million in the **Capital Development category from the Infrastructure Fund** (*Tasi Mane Project*) for most of the current expenses. Prudence in the management of public funds, advising against such a policy option, since the funds for capital development are of vital importance for the economic and social development of the country in terms of its basic infrastructure.

Table III - Additional expenditure in the Rectification state budget for:

Additional expenditure of more than $1 million	Amount (Millions of dollars)
Pension for Veterans	26.9
Allowance for Elderly	7.1
Contingency Fund	6.1
Ministry of Defense and Security	2.9
Ministry of Education, School of Rehabilitation	1.7
Goods and Services for PNTL	2.4
Transfer to the Church and Civil Society in Prime Minister's office	1.4
Ministry of Health	1.2
Goods and Services for the operation of Berlin - Nakroma	1.2
Minor Capital for Water	1.2
Goods and Services for the Institute of Equipment	1.2
External Audit	1.1
Payment for LIFESEA (sic) the Secretary of State for Defense	1.1
All other expenses (net) of CFTL	-5.4
TOTAL	**50.1**

By analyzing the table 2.1.1 of the Rectification budget Book for 2012, there is the intention to strengthen in $26.9 million from the budget line **"Pensions for Veterans,"** which raises the possibility that the Government, in preparing the General State Budget for 2012, significantly underestimated the cost of this item. An increase of this magnitude requires a thorough and reasoned explanation from the Government.

In the public hearings, the Hon. Finance Minister justified this expense increase, based on the final tabulation of data by the Verification Committee constituted for the purpose, which will have to count a number of veterans much higher than originally anticipated when preparing the 2012State Budget. Given the relatively high budget, which stands at $26.9 million, the Government should make available to

Parliament, during the general debate, all the information needed to assess the justification for the additional expense now foreseen. Moreover, it is worth asking whether, having reached that amount it will be possible to execute the whole amount in a relatively short period (three months).

Also strengthening of the budget line "**Allowance for Seniors**" at $7.1 million deserved consideration for the same reasons as the increased allocation for Pensions for Veterans, that is, an incorrect amount at the time of allocation of funds in the State Budget for 2012.

We emphasize the creation, in the proposed rectification budget under review, a budget line called **"Office of the First Lady"** within the Presidency of the Republic, with a budget of $50,000 , for an execution scheduled just about 3 months taking place until the end of 2012. Given this proposal, may raise the question of whether the creation of that office has enough legal sustenance or not, the current legal framework, considering whether this option is better discussed during the general debate on the proposal.

The category of **"Goods and Services" for the National Police of Timor-Leste (PNTL)** will also benefit from a substantial increase, according to the government proposal, amounting to $2.4 million. It would be better to understand the nature of the deviations in the implementation of that budget category and the urgent reasons leading to PNTL's need to purchase new vehicles by the end of the year, instead of including this expense in the State Budget for 2013. The allocation to the category of goods and services for PNTL had a balance, on August 8, 2012, of $2.1 million.

The **Contingency Fund**, required with an additional $6.1 million, also deserves some consideration. Pursuant to Article 38 of the Budget and Financial Management Law, contingency expenses are due to "urgent and unforeseen needs" normally associated with natural disasters, such as floods, fires, landslides, etc., that is, situations impossible to predict and that could pose serious risks. This does not seem to be the case in the Rectification Budget for 2012, the explanations seem insufficient so far provided by the government to justify the additional expense projection to include. About this item is therefore necessary to clarify in detail by the Hon. Minister of Finance, supported by an identification of expenses already incurred on behalf of the Fund.

Note that the allocations under *contingency* item(s) and their implementation are greater than what would be desirable in view of its nature and because, as the name indicates, it is to allocate funds to cover *unpredictable, urgent and unavoidable costs*, the amounts entered under this heading should never be used for various purposes, or which may occur without those assumptions. Thus, we reiterate the recommendation that has come to be formulated by Parliament and by this Committee in particular, to ensure judicious management of the funds in question.

The Government notes the need, through the Rectification Budget for 2012, to make some adjustments to appropriations lines within the various categories of recurrent expenditure, totaling $5.4 million, justifying it on the basis of the change in organizational structure. Considering their relative size may raise the question whether perhaps the new structure will not translate into greater systemic entropy, in a context where it would be desirable to ensure greater coherence and coordination in public administration.

The **Human Capital Development Fund** has a balance of $7.4 million at the end of 2011, which the Government chooses not to integrate in this Rectification Budget, however reserving "the right to add the amount not spent" if needed, until the end of the year. This Government's determination leads to the conclusion that there are two weights and measures for the integration of balances carried forward from Special Funds, and that this is an opportune time for the Government, in the first budget amendment to the State Budget for 2012, to integrate the balances of the Infrastructure Fund and HCDF. The Executive can always safeguard the revenue savings from the integration of additional balances under consideration, through blocking these funds until the end of the year and, with this methodology, increase transparency and budgetary rigor, providing regular and updated reporting to Parliament on the totality of available funds in state coffers.

Noting the enrollment of $1.1 million to "**Pay for LIFESEA (sic) the State Secretariat of Defense**," in the process of building the floating dock at Hera, the Committee considers to be necessary clarifications about all relevant aspects of the contractual process in question, to be provided by the Government in the general debate.

Finally, given the justification given by the Government for the reduction of 5.4% in "**All Other Expenses (net) CFTL**" that, in most cases, new divisions have a budget of $58,000 for Salaries and Compensation and $43,000 for Goods and Services, it is worth asking whether the planning of ministry operating expenses was performed according to their relative weight and consistent with the strategic priorities of the Government for 2012 and also whether all state agencies who suffered budget changes have been consulted in advance about the decision to reduce their allocations in the Rectification Budget.

CAPITAL EXPENDITURES

Capital expenditures are distributed in the State Budget for the categories of "Minor Capital" and "Development Capital". We found both categories of expenditure in the budget of the Consolidated Fund of Timor-Leste (CFTL) for most Ministries and also the Infrastructure Fund.

The allocation in the State Budget for capital expenditures is primarily aimed at the acquisition of durable equipment and the production of infrastructure essential for economic development, so the Government's intention to withdraw $50 million from the **Infrastructure Fund** budget to boost recurring items of expenditure should be reconsidered, so as not to call into question the strategy of development of the country, as previously noted.

The execution of the Infrastructure Fund, as of 8 August 2012, did not exceed 41%, when it should be within about 60% for the period under review, by which is meant to be requesting additional information about the reasons as reduced performance and assess possible responsibilities, of the Government or contracted companies, for delays in completion of projects contained therein.

Noting a negative balance of $113 thousand on the project "Protection of Tono Irrigation Canal and the Agricultural Zone irrigation scheme," expressed in the table of the Infrastructure Fund appearing in the Budget Execution Report of August 8, 2012, which is not acceptable to the fiscal rules that any project exceeds the annual appropriation approved and entered in the State Budget, for any item or project.

6. RECOMMENDATIONS AND CONCLUSIONS

RECOMMENDATIONS

1. Given the increased difficulties in reading and interpreting budget charts and tables, resulting from lack of information and data systematization, the Committee recommends more rigor in the future, regarding the numerical representation and decimals used sufficiently clear identification of monetary units (legend) and use in the budgetary tables economic and financial terminology in our own official language in place of English expressions or mismatched categories for usual techniques (e.g. *virements, roll over, recurring costs,* etc.).

2. It is recommended that the Government avoid recourse to the balance carried over from the category of Development Capital in the Infrastructure Fund to support additional current expenditure under Rectification Budget for 2012, as these funds are allocated and are necessary for the implementation of ongoing capital development projects;

3. The Government has been requesting reassignment to additional current expenditure in various other categories of spending, an amount of $1.25 million, previously entered under the category Salaries and Wages. It is recommended that the Government use greater rigor in the estimates of future financial needs and/or better budget planning, to avoid budgetary changes of this nature;

4. Taking into account the possible effects of public spending on the price levels of goods and services in

the internal market, it is recommended that specific monitoring the evolution of the consumer price index (CPI), which can go for updating the market basket of goods and the quarterly collection of statistical information on the basket set, to analyze the evolution of domestic inflation. This recommendation was included in the Report and Opinion of the Committee C of the proposed State Budget for 2012, but the situation remains unchanged so far, according to available information;

5. We also reiterate the recommendation already made in the Report and Opinion on Proposed State Budget for 2012, the urgent adoption of the Official Public Accounts, in compliance with art. 10 of Law no. 13/2009 of 21 October;
6. It is recommended that there be greater coordination between the various ministries, the ADN, the CNA and the Major Project Secretariat, and that each ministry is the executor of major projects relating to them;
7. It is recommended greater collaboration between the Ministries concerned and Development Partners, for identification and judicious allocation of financial resources;
8. Considering the reduced or even zero level implementation of some investment projects in infrastructure, until August 8, 2012, recommended to the Government to review the policy and procedures for monitoring and control in this area;
9. It is recommended that adoption be considered, as soon as possible, of urbanization plans, including for the city of Dili, considering future needs in terms of infrastructure and its respective implications for the financial plan;
10. It is recommended to be traded and contracted a clear plan of maintenance for State vehicles, duly detailed and ensuring a more efficient and transparent public resource allocation;
11. It is recommended that the Government take steps to regularize debts to hospitals in Indonesia and Singapore, contracted under protocols agreed by the Government to assist the Timorese patients. It is also recommended that the Government promote the development of domestic supply in the health sector, and particularly in the short term by improving the facilities and equipment of Guido Valadares National Hospital and ensuring qualified human resources, thus less reliance on health services abroad.

CONCLUSIONS

The draft rectification budget for 2012 submitted by the Government to the National Parliament on 14 September 2012, provides for an increase of overall expenditure budget for 2012 of more than $124.9 million, corresponding to the balance carried over from 2011 , the various projects of the Infrastructure Fund. Pursuant to Article 13 of Decree-Law no. 8/2011, of 16 March, regulating the Infrastructure Fund (IF), balances at the end of 2011 are retained by the Fund in the relevant official account, moving automatically to 2012. However, pursuant to paragraphs 5 and 6 of Article 32 of the Budget and Financial Management Law, all expenses incurred by the Fund must be authorized by the Finance Minister, which authorization may be issued only if estimates of revenue and expenditure of the fund for the financial year are presented to the National Parliament. Given the above, although the IF has been reinforced with $124.9 million, the government can execute the balance of 2011 when they have presented to the National Parliament estimates of revenue and expenditure of the Fund for the financial year 2012.

At a time when the country needs to implement large-scale projects for development and modernization, it is essential to avoid the errors associated with the process of installing the port of Hera. All contracts awarded by the state, must should be reviewed in detail and necessary preliminary technical studies conducted to ensure that any major work done will not cause negative environmental impacts.

The Bebui Watulari irrigation project has been completed for over a year, so it is essential that the Government clarify fully the reason why, the budget for 2012 contains $1.337 million for this project and did not use this proposed budget amendment to adjust the appropriation to reality.

Finally, we should recommend to the Government that passes to include in their budget proposals the assessment of economic, social and environmental impacts within the population, their economic, financial and tax.

7. OPINION

The Committee on Public Finance is thus of the opinion that Proposed Law 1/III - First Amendment to Law no. 16/2011 of 21 December, approving the State Budget for 2012, meets the constitutional, legal and regulatory requirements, and is therefore able to advance to the plenary for general and specific discussion and voting, reserving the parliamentary parties their positions to debate.

The opinions and recommendations of all other specialized committees, are an integral part of this report and are listed in Annex 2 to this Report and Opinion of the Committee of Public Finance.

8. ADOPTION OF THE REPORT AND OPINION

This report and opinion was discussed and approved at the meeting on 9 October 2012, by 7 votes in favor, 4 against and 0 abstentions.

Dili National Parliament on 09 October 2012

The Rapporteurs

(Maria Adozinda Pires da Silva)

(Maria Fernanda Lay)

Committee President

(Virgílio Maria Dias Marçal)