



REPÚBLICA DEMOCRÁTICA DE TIMOR-LESTE
MINISTÉRIO DO PLANO E DAS FINANÇAS
GABINETE DA MINISTRA

PETROLEUM FUND 2005-06 ANNUAL REPORT

The Petroleum Fund of Timor-Leste was established under the provisions of the Petroleum Fund Law no 9/2005, on 3 August 2005. The Banking and Payments Authority of Timor-Leste (BPA) is responsible for the operational management of the Fund, in accordance with a Management Agreement dated 12 October 2005 between the Ministry of Planning and Finance and the BPA.

The first investments of the Petroleum Fund started on 9 September 2005 when USD 79.6 million US dollars were transferred from the Timor Gap Account together with 125 million US dollars from the Consolidated Fund of Timor-Leste (CFET). Taxes and other petroleum revenue totaling 438.2 million US dollars were paid to the Petroleum Fund during the year ended 30 June 2006.

In accordance with the Management Agreement the Fund is invested in debt instruments issued by the Government of the United States. The investments shall track the 0-5 year government bond index (Merrill Lynch). The mandate of BPA is to keep the duration of the portfolio within a range of +/- 0.2 year of this benchmark portfolio.

The return on investments during the year was 7.3 million US dollars after taking account of revaluation losses. The market value of the Petroleum Fund as of 30 June 2006 was 649.8 million US dollar. In accordance with the Management Agreement, a management fee to BPA of 270,000 US dollar has been withdrawn from the Petroleum Fund.

In accordance with the accounting policies of the Petroleum Fund the accounts will show a loss on the investments when the market interest rates are increasing, and a gain when market rates are falling. During the reporting period market rates have increased, causing a loss of 5.8 million US dollars. As the bonds generally will be held to maturity this loss will not be realized.

The average yield to maturity of the investments made through the period 9 September 2005 through 30 June 2006 have been estimated at 4.6 per cent. During the period from September 2005 to June 2006 inflation in US was 3.2 per cent, the real return on the investments, based on the yield to maturity, is accordingly 1.4 per cent.

The BPA has managed its investment mandate in accordance with the Management Agreement. The yield on the portfolio has generally been in line with the yield on the benchmark portfolio (there is a difference in favor of the benchmark of 0.03 percentage points).

The Government has not made any withdrawal from the Petroleum Fund during the 2005-06 Budget year.

The Investment Advisory Board of the Petroleum Fund had its first regular meeting on 17 January 2006 and subsequently met on 18 April 2006. The minutes from the meetings are available on www.bancocentral.tl .

Deloitte Touche Tohmatsu was appointed Independent Auditor of the Petroleum Fund in August 2006. Deloitte Touche Tohmatsu has produced two separate reports in accordance with the Article 35 of the Petroleum Fund Law and Guidelines for Extractive Industries Transparency Initiative (EITI). These reports are attached with this document and are also available at www.transparency.gov.tl and at www.mopf.gov.tl

Signed on 14 of May 2007

Maria Madalena Brites Boavida
Minister for Planning and Finance

Annexes:

Audited Financial Statements

Statement from the Deputy Director of Treasury

Comparison of income with previous three years

Comparison of nominal income to real returns

Comparison of income with benchmark

Comparison of Estimated Sustainable income with transfers from the Petroleum Fund

Statement on borrowings

A list of persons holding positions relevant for the operations and performance of the Petroleum Fund

Article 35 report on Petroleum Fund Receipts from Delotte Touche Tohmantsu

EITI report from Deloitte Touche Tohmatsu

PETROLEUM FUND OF TIMOR-LESTE

FINANCIAL STATEMENTS

FOR THE YEAR ENDED

30 JUNE 2006

**DIRECTOR OF TREASURY
MINISTRY OF PLANNING AND FINANCE**

Director's Report

The Petroleum Fund Law No. 9/2005 was promulgated on 3 August 2005 and it established the Petroleum Fund of Timor-Leste. Prior to establishment of Petroleum Fund, the tax revenues pertaining to petroleum activities were part of the general Consolidated Fund of Timor-Leste (CFET) while the petroleum royalties were held in a separate Timor Gap Account with Banking and Payments Authority of Timor-Leste (BPA).

BPA is responsible for the operational management of the Fund, in accordance with a Management Agreement dated 12 October 2005 between the Ministry of Planning and Finance and the BPA. BPA has also responsible for maintaining the books of account for the Fund on behalf of the Director of Treasury. In accordance with Article 21 of the Petroleum Fund Law, the financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). The statements are:

*Income statement,
Statement of changes in capital,
Balance Sheet,
Cash flow statement, and
Notes to accounts*

The accounts and the financial statements have been externally audited by Deloitte, Touche & Tohmatsu whose audit opinion is attached with this report.

The Petroleum Fund received an initial capital of USD 204.6 million on 9 September 2005 by way of transfer of balance under Timor Gap Account of USD 79.6 million together with USD 125 million from the CFET. For the period ending 30 June 2006, taxes and other petroleum revenue totaling USD 438.2 million were received in the Petroleum Fund making the gross receipts of USD 642.8 million.

The Fund earned a profit of USD 7.0 million during the year (refer to the "Income Statement"). The capital of Fund as on 30 June 2006 was USD 649.8 million.

A summary of the transactions is given in the "Statement of changes in capital".

During the course of fiscal year, Ministry of Planning and Finance together with the Banking & Payments Authority have been able to accomplish the stewardship and fiduciary role for the Petroleum Fund.



(Manuel Monteiro)

Deputy Director of Treasury
Ministry of Planning & Finance

Income Statement**For the year ended 30 June 2006**

	<i>Note</i>	US Dollars 2006
Investment income		
Interest on investments	3	13,149,815
Gains and losses on investments		
Gains/(losses) on fair value through profit or loss assets	5	(5,831,519)
Total investment income		<hr/> 7,318,296
<i>Less:</i>		
Management Fee		270,000
Profit for the year		<hr/> 7,048,296 <hr/>

The above statement is to be read in conjunction with the notes on pages 5 to 22

Statement of changes in capital**For the year ended 30 June 2006**

	<i>Note</i>	US Dollars 2006
Capital at 1 July 2005		-
Transfers to the Petroleum Fund pursuant to Article 6 of the Petroleum Fund Law		
<i>Transfers from the Consolidated Fund and Timor Gap Account</i>		204,603,705
<i>Petroleum Fund gross receipts</i>		438,196,227
Total transfer to Petroleum Fund	6	<u>642,799,932</u>
Transfers to the Consolidated Fund pursuant to Article 7 of the Petroleum Fund Law		-
Refunds of taxation pursuant to Article 10 of the Petroleum Fund Law		-
Profit for the year		7,048,296
Capital at 30 June 2006		<u><u>649,848,228</u></u>

The above statement is to be read in conjunction with the notes on pages 5 to 22

Balance Sheet**As at 30 June 2006**

US Dollars

	<i>Note</i>	<i>2006</i>
ASSETS		
Cash and cash equivalents	8	499,284
Interest receivable	4	3,215,759
Receivables for pending sales of investments	9	-
Investments at fair value through profit or loss	5,11	646,133,185
TOTAL ASSETS		649,848,228
LIABILITIES		
Payable for pending purchases of investments	9	-
TOTAL LIABILITIES		-
NET ASSETS		649,848,228
Capital		
Capital		649,848,228
TOTAL CAPITAL		649,848,228

The above statement is to be read in conjunction with the notes on pages 5 to 22

Cash Flow Statement**For the year ended 30 June 2006**

	<i>Note</i>	US Dollars 2006
<i>Cash flows from operating activities</i>		
Interest received		9,934,056
Operating expenses paid		(270,000)
Cash flow from operating activities	18	9,664,056
<i>Cash flow from investing activities</i>		
Proceeds from sale of investments	5	259,255,492
Purchase of investments	5	(911,220,197)
Cash flow from investing activities		(651,964,705)
<i>Cash flow from funding activities</i>		
Transfer from Government		204,603,705
Petroleum Fund Receipts		438,196,227
Transfer to Consolidated Fund		-
Cash flow from funding activities	6	642,799,932
Increase/(Decrease) in Cash and Cash equivalents for the year	8	499,284
Cash and cash equivalents at 1 July 2005		-
<i>Cash and cash equivalents at 30 June 2006</i>		499,284

The above statement is to be read in conjunction with the notes on pages 5 to 22

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1. General Information

The Petroleum Fund of Timor-Leste (the ‘Petroleum Fund’) was established under the provisions of the Petroleum Fund Law No. 9/2005 of the Democratic Republic of Timor-Leste enacted on 3 August 2005.

Pursuant to Article 139 of the Constitution of the Republic, petroleum resources are owned by the State and are to be used in a fair and equitable manner in accordance with national interests, with the income derived there from leading to the establishment of mandatory financial reserves. The Petroleum Fund is a means of contributing to the wise management of petroleum resources for the benefit of both current and future generations, and a tool that contributes to sound fiscal policy where appropriate consideration and weight is given to the long-term interests of Timor-Leste’s citizens.

The Banking and Payments Authority of Timor-Leste (BPA), having its office at Avenida Bispo Medeiros, Dili, Timor-Leste, is responsible for operational management of the Petroleum Fund, and is the registered owner of all the assets of the Petroleum Fund. The management of the Petroleum Fund is undertaken according to a Management Agreement between the Ministry of Planning and Finance and the BPA signed on 12 October 2005.

These are the first financial statements of the Petroleum Fund covering the financial year from 3 August 2005 to 30 June 2006. Accordingly, there are no comparative figures.

The financial results and balances reported in these financial statements are not rounded.

These financial statements were authorized for issue by the Director of Treasury on May 2007.

2. Significant Accounting Policies

Basis of accounting

In accordance with Article 21 of the Petroleum Fund Law, the financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) which comprise standards and interpretations approved by the International Accounting Standards Board (IASB) and International Accounting Standards and Standing Interpretations Committee interpretations approved by the International Accounting Standards Committee (IASC) that remain in effect at the Petroleum Fund's balance date.

The financial statements are presented in United States dollars. They are prepared on the historical cost basis, except for the revaluation of certain financial instruments.

The preparation of financial statements in conformity with international accounting standards requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expense. The estimates and associated assumptions are based on historical experience and other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values and assets and liabilities that are not readily apparent from other sources. Actual results may vary from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision, and future periods if the revision affects both current and future periods.

Judgments made by management in the application of international accounting standards that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 12.

The accounting policies have been consistently applied by the Petroleum Fund. The Petroleum Fund has adopted the IFRSs that were effective at balance date. The Petroleum Fund has also adopted *IFRS 7: Financial Instruments Disclosures* although the effective date for the standard is 1 January 2007.

The Petroleum Fund invests in financial markets in the United States of America. The Petroleum Fund is organized and operates as one segment (both in terms of business and geography). Consequently, no segment reporting is provided in the Petroleum Fund's financial statements.

The balance sheet presents assets and liabilities in increasing order of liquidity and does not distinguish between current and non current items.

The principal accounting policies are set out below.

(a) Foreign currency translation

(i) Functional and presentation currency

Items included in the Petroleum Fund's financial statements are measured using the currency of the primary economic environment in which it operates. This is the United States Dollar, which reflects the Petroleum Fund's primary activity of investing in US securities. This is also the currency of presentation as it is the official currency of the Democratic Republic of Timor-Leste.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement.

(b) Financial instruments

(i) Classification

Investments

The manner in which the Petroleum Fund is managed and its performance measured is set out in Annex 1 to the Operational Management Agreement signed by the Minister of Planning and Finance and the General Manager of the Banking & Payments Authority on 12 October 2005. The Merrill Lynch 0-5 year government bond index is established therein as the performance benchmark, with the requirement that the Petroleum Fund be managed passively with the objective of achieving a return within 25 basis points while maintaining the modified duration of the investment portfolio within 0.2 years of the benchmark.

The investment portfolio of the Petroleum Fund, being managed and having its performance measured and reported in accordance with these documented risk management and investment strategies, has accordingly been designated at fair value through profit or loss for accounting purposes.

Interest and other receivables

Financial assets that are classified as loans and receivables include cash balances due from financial intermediaries from the sale of securities, receivables from reverse repurchase agreements with a maturity of more than one business day, and accounts receivable.

Financial liabilities that are not at fair value through profit and loss include balances payable to financial intermediaries for the purchase of securities, and accounts payable.

*(ii) Recognition and de-recognition**Investments*

The Petroleum Fund recognizes financial assets and financial liabilities on its balance sheet from the date the Petroleum Fund becomes a party to the contractual provisions of the instrument. The Petroleum Fund offsets financial assets and financial liabilities if the Petroleum Fund has a legally enforceable right to set off the recognized amounts and interests and intends to settle on a net basis.

Investments are derecognized when the rights to receive cash flows from the investments have expired or the Petroleum Fund has transferred substantially all risks and rewards of the ownership.

Financial liabilities are derecognized when the obligation specified in the contract is discharged or cancelled or expired.

Interest and other receivables

Other receivables and payables are recognized on an accruals basis.

*(iii) Measurement**Investments*

Financial instruments are measured initially at fair value.

Investments are designated at fair value through profit or loss on initial recognition. As the Petroleum Fund's business is investing in financial assets according to a defined mandate with a view to profiting from their total return in the form of interest, dividends or increases in fair value, listed securities and fixed income securities are designated as fair value through profit and loss on initial recognition.

The Petroleum Fund manages and evaluates the performance of these investments on a fair value basis in accordance with its investment mandate, with information about the performance of the investments and their related benchmarks being regularly published.

Financial assets designated as at fair value through profit and loss are measured at subsequent reporting dates at fair value, based on the bid price.

Changes in the fair value of such investments (including impairment losses and foreign exchange gains and losses) are recognized in the income statement until the financial asset is derecognized.

Interest and other receivables

Other receivables do not carry interest and are short-term in nature and accordingly are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts.

(iv) Impairment

Financial assets that are stated at cost or amortised cost are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such indication exists, an impairment loss is recognized in the income statement as the difference between the asset's carrying amount and the present value estimated future cash flows discounted at the original effective interest rate.

If in a subsequent period the amount of an impairment loss recognized on a financial asset carried at amortised cost decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down is reversed through the income statement.

(v) Fair value measurement principles

The fair value of financial instruments is based on their quoted market prices at the balance sheet date without any deduction for estimated future selling costs. Financial assets held or a liability to be issued are priced at current bid prices, while financial liabilities held and assets to be acquired are priced at current asking prices.

(vi) Specific instruments

Cash and cash equivalents

Cash comprises current deposits with banks. Cash equivalents are short-term highly liquid investments that are readily convertible to known amounts of cash, are subject to an insignificant risk of changes in value, and are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes.

Repurchase and reverse repurchase transactions

Securities sold subject to a simultaneous agreement to repurchase these securities at a certain later date at a fixed price (repurchase agreements) are retained in the financial statements and are measured in accordance with their original measurement principles. The proceeds of sale are reported as liabilities and are carried at amortised cost.

Securities purchased under agreements to resell (reverse repurchase agreements) with a maturity period of greater than one financial day are reported not as purchases of securities, but as receivables and are carried in the balance sheet at amortised cost.

Interest earned on reverse repurchase agreements and interest incurred on repurchase agreements is recognized as interest income or interest expense over the life of each agreement using the effective interest method.

(vii) Encumbrances on the assets of the Petroleum Fund

The Petroleum Fund is not permitted to encumber its assets. In accordance with Article 20 of the Petroleum Fund law any contract, agreement, or arrangement, to the extent that it purports to encumber the assets of the Petroleum Fund, whether by way of guarantee, security, mortgage or any other form of encumbrance, is null and void.

(c) Recognition of Petroleum Fund Receipts

The Petroleum Fund Law requires certain parties to deposit taxes and other petroleum-related payments payable to the Government of Timor-Leste directly into the Petroleum Fund. The Petroleum Fund recognizes these and other transactions affecting the capital of the Petroleum Fund as follows:

- Payments made as Petroleum Fund receipts in accordance with Article 6.1(a) are recognized as income in the State accounts, and accordingly are credited directly to the capital account of the Petroleum Fund.
- Payments made by the Designated Authority in accordance with Article 6.1(b) are recognized as income in the State accounts, and accordingly are credited directly to the capital account of the Petroleum Fund.
- Income earned by the Petroleum Fund from the investment of its assets is recognized in the Income Statement and credited to the capital of the Petroleum Fund in accordance with Article 6.1(c).
- Management fees paid from the gross receipts of the Petroleum Fund pursuant to Article 6.2 are recognized in the Income Statement.
- Refunds of taxation made pursuant to Article 10 are shown as reductions in the capital of the Petroleum Fund.

(d) Interest income

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's carrying amount.

(e) Expenses

In accordance with the provisions of the Petroleum Fund Law, all expenses of the Petroleum Fund, not relating to the purchase or sale of securities and recognized in the sale or purchase price, are met by the Banking and Payments Authority of Timor-Leste and are covered by a management fee.

In accordance with Article 6.3 of the Petroleum Fund Law, the management fee paid to the Banking and Payments Authority is recognized as a deduction from the gross receipts of the Petroleum Fund, although it is accounted in the income statement of the Petroleum Fund. Management and performance fees payable to external fund managers are met from the management fee payable to the Banking and Payments Authority.

Expenses which are incidental to the acquisition of an investment are included in the cost of that investment.

Expenses that are incidental to the disposal of an investment are deducted from the disposal proceeds of the investment.

(f) Taxation

The Petroleum Fund is exempt from paying taxes on income, profits or capital gains under the current system of taxation in the Democratic Republic of Timor-Leste.

3. Interest Income

Interest was earned during the year from the following sources:

	US Dollars 2006
Fixed interest debt securities	12,897,038
Cash and cash equivalents	<u>252,777</u>
	<u>13,149,815</u>

4. Interest Receivable

The amount of interest accrued at balance date was as follows:

	US Dollars 2006
Cash and cash equivalents	75
Fixed interest debt securities	<u>3,215,684</u>
	<u>3,215,759</u>

5. Financial Assets

Aside from short-term cash management activities, the Petroleum Fund has invested solely in United States Government Treasury Notes from its inception to balance date. Sales of securities have taken place to periodically rebalance the investment portfolio to the benchmark.

Investments

US Dollars

2006

Fair value through profit or loss assets

Opening cost at 1 July 2005	-
Gains/(losses) at 1 July 2005	-
Opening fair value	-
Purchases at cost	911,220,197
Proceeds from sales	(259,255,492)
Realised losses on sale	(1,078,179)
Cost of investment assets at 30 June 2006	650,886,526
Unrealised losses at balance date	(4,753,340)
Fair value of investment assets at 30 June 2006	646,133,186

Gains and losses on investments**Realised gains/(losses)**

Realised gains	91,473
Realised (losses)	(1,169,652)
	(1,078,179)

Unrealised gains/(losses)

Unrealised gains	50,223
Unrealised (losses)	(4,803,563)
	(4,753,340)

Net (loss) on investments**(5,831,519)**

There were no impairment losses at balance date.

The carrying amount of these assets approximates their fair value.

6. Transfers to the Petroleum Fund

The following table analyses the payments made as Petroleum Fund receipts by month of receipt:

Month	US Dollars				
	2006				
	Article 6.1(a) receipts	Article 6.1(b) receipts	From Consolidated Fund	From Timor Gap Account	TOTAL
August 2005	17,717,611	-	-	-	17,717,611
September	19,509,978	6,254,198	125,000,000	79,603,705	230,367,882
October	36,230,768	8,528,638	-	-	44,759,406
November	39,907,971	8,814,415	-	-	48,722,386
December	19,715,931	7,394,969	-	-	27,110,900
January 2006	23,601,290	6,335,360	-	-	29,936,650
February	42,318,414	6,362,061	-	-	48,680,475
March	50,843,155	6,967,263	-	-	57,810,418
April	35,379,185	10,846,282	-	-	46,225,467
May	31,819,990	7,666,912	-	-	39,486,902
June	43,680,184	8,301,651	-	-	51,981,835
Totals	360,724,477	77,471,749	125,000,000	79,603,705	642,799,932

The transfer of US\$125 million to the Petroleum Fund from the Consolidated Fund of Timor-Leste on 9 September 2005 was effected in accordance with a decision of the Council of Ministers. The transfer of US\$79.6 million represents the accumulated balance of the "Timor Gap" account established at the Banking and Payments Authority in 2000, the balance of which represents First Tranche Petroleum royalties plus interest earned on the account from 1999 up to the date of the transfer.

7. Payments to State Budget Account

As per Article 7 of the Petroleum Fund Law, the only debits permitted to the Petroleum Fund are electronic transfers to the credit of a single State Budget account. The total amount transferred from the Petroleum Fund for a Fiscal Year must not exceed the appropriated amount approved by Parliament for the year.

During the year ended 30 June 2006 no appropriation was made from the Petroleum Fund by parliament, nor were any transfers made from the Petroleum Fund to the State Budget account.

8. Cash and Cash Equivalents

Prior to investment the Petroleum Fund places surplus cash in the New York overnight money market through reverse repurchase agreements. For the purposes of the cash flow statement, cash and cash equivalents comprise the following balances with original maturity of less than 90 days:

US Dollars

	2006
Cash at bank	299,284
Overnight reverse repurchase agreements	<u>200,000</u>
	<u>499,284</u>

The cash at bank represents the balance at the Federal Reserve Bank of New York, in the earmarked receipts account held by the BPA in accordance with Article 5.2 of the Petroleum Fund Law.

The carrying amount of cash and cash equivalents approximates their fair value.

9. Receivables and Payables for Pending Sales and Purchases of Investments

In accordance with the Petroleum Fund’s policy of trade date accounting for regular way sale and purchase transactions, sales/purchases awaiting settlement represent amounts receivable/payable for securities sold/purchased, but not yet settled.

	US Dollars
	2006
Receivables	
Pending sales of investments	-
 Payables	
Pending purchases of investments	-

The carrying amount of these assets and liabilities approximates their fair value.

10. Related Party Transactions

The ultimate controlling party of the Petroleum Fund is the Democratic Republic of Timor-Leste.

The following are related parties:

- (a) The government, as stipulated in Article 11.1 of the Petroleum Fund Law, is the manager of the Petroleum Fund.

The Petroleum Fund receives revenues on behalf of the government, as disclosed in note 2(c). The government, through the State budget, meets the expenses of the Petroleum Fund, including the audit fee, not otherwise covered by the management fee.

- (b) The Banking and Payments Authority of Timor-Leste is the operational manager of the Petroleum Fund, in accordance with Article 11 of the Petroleum Fund Law.

The Government entered into a management agreement with BPA on 12 October 2005 for the operational management of the Petroleum Fund. The management agreement provides the Banking and Payments Authority a management fee of US\$270,000, which reasonably represents the Banking and Payments Authority's cost of managing the Petroleum Fund, for the 2006 fiscal year. The management fee has been drawn in equal monthly instalments.

11. Qualifying Instruments

All financial assets are designated by the Petroleum Fund as at fair value through profit or loss upon initial recognition. In accordance with the provisions of Article 24.1(a) of the Petroleum Fund Law the qualifying instruments of the Petroleum Fund at 30 June 2006 were as follows

US Treasury Notes		US Dollars		
		Face Value	Fair Value	% of net assets
3½%	15 Nov 2006	152,300,000	151,329,848	23.4
4¾%	15 May 2007	104,600,000	103,798,765	16.1
3%	15 Nov 2007	93,600,000	90,875,301	14.1
2½%	15 May 2008	72,800,000	69,515,263	10.7
3¾%	15 Nov 2008	56,300,000	54,087,410	8.4
3¾%	15 May 2009	53,600,000	51,814,047	8.0
3½%	15 Nov 2009	40,500,000	38,495,251	6.0
3¾%	15 May 2010	33,700,000	32,250,562	5.0
4½%	15 Nov 2010	36,300,000	35,457,477	5.5
4¾%	30 April 2011	18,700,000	18,509,261	2.8
Total		662,400,000	646,133,185	100.0%

12. Critical Accounting Estimates and Judgements

The Petroleum Fund makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates are continually evaluated and based on historical experience and other factors, including expectations of the future events that are believed to be reasonable under the circumstances.

Estimates use observable data to the extent practicable. However, areas such as credit risk, volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

The Petroleum Fund has made a judgement that investments should be recognized on a fair value through profit or loss basis (rather than using the "available for sale" basis) and income recognized accordingly, because the performance of the Petroleum Fund is measured and reported on a fair value through profit or loss basis for the reasons outlined in Note 2(b)(i).

Judgements have been made as to whether certain transactions should be recognised as capital or revenue. The basis for these judgements is outlined in Note 2(c).

13. Risk Management

Investment Strategy

The Petroleum Fund's objective is to meet benchmark returns on its capital in accordance with the management agreement and within the limits established in Articles 14 and 15 of the Petroleum Fund Law relating to Investment Rules and Qualifying Instruments.

The Rules provide that not less than 90% of the amounts in the Petroleum Fund shall be invested only in the qualifying instruments and the balance may be invested in other financial instruments that are issued abroad, are liquid & transparent, and are traded in a financial market of the highest regulatory standard.

The Rules further provide that a qualifying instrument is:

- (a) an interest bearing debt instrument in US dollars which is rated Aa3 or higher by Moody rating agency or AA- or higher by Standard & Poor's rating agency, or is issued by or guaranteed by World Bank or a sovereign state (other than Timor-Leste) provided the issuer or guarantor is rated as above; or
- (b) interest bearing US dollar denominated debt instrument or US dollar deposit issued by Bank for International Settlements, or European Central Bank, or central bank of a sovereign state (other than Timor-Leste) or any other bank with a long term currency ratings as above.
- (c) A derivative instrument which is solely based on (a) or (b) above provided its acquisition reduces the financial exposure to the risks associated with the underlying instruments.

Furthermore, the average interest rate duration of the qualifying instruments shall be less than 6 years.

These Articles in the law, together with the mandate in the Operational Management Agreement, define the framework within which risks are to be managed.

The interest rate duration (modified duration) of the benchmark and the portfolio at 30 June 2006 was 1.71 years.

The Petroleum Fund did not enter into any transactions of a derivative nature during the period covered by these financial statements, whether for hedging purposes or otherwise.

The Petroleum Fund investment portfolio of assets at fair value through profit or loss (excluding cash and cash equivalents) complied with the legislative and contractual requirements outlined above throughout the year.

The financial risks associated with the Petroleum Fund are monitored by the Risk Management Division of the Petroleum Fund Department at the Banking and Payments Authority, which prepares daily reports for senior management. The Petroleum Fund is subject to periodic audit

by the Internal Audit Office of the Banking and Payments Authority, which has operational independence from the management of the Petroleum Fund. The Internal Audit Office provides formal monthly reports to the General Manager, and quarterly reports to the Governing Board of the Banking and Payments Authority.

13. Operational Risk

Operational risk is the risk of loss in both financial and non-financial terms resulting from human error and the failure of internal processes and systems.

The Banking and Payments Authority, as the operational manager of the Petroleum Fund, manages the operational risks associated with the operations of the Petroleum Fund. Operational risk management includes corporate policies that describe the standard of conduct required of staff, and specific internal control systems designed around the particular characteristics of the Petroleum Fund.

Compliance with corporate policies and departmental internal control systems are managed by an active internal audit function, and specific provision in the daily reports prepared by the Risk Management Division for the reporting of all issues that arise in connection with operational matters. The purpose of this section of the reports is to notify senior management promptly of unexpected operational issues, and provide them with the opportunity to provide advice or take remedial action.

14. Credit Risk

Credit risk is the risk of loss arising from counterparty to a financial contract failing to discharge its obligations.

(a) Credit risk management

The framework for managing credit risk is broadly provided for in Article 15 of the Petroleum Fund Law, which states that the only instruments that may be acquired by the Petroleum Fund are interest bearing debt instrument in US dollars which are rated Aa3 or higher by Moody rating agency or AA- or higher by Standard & Poor's rating agency, or are issued by or guaranteed by World Bank or a sovereign state (other than Timor-Leste) provided the issuer or guarantor is rated as above.

In recognition of the mandate in the Operational Management Agreement that the performance of the Petroleum Fund will be measured against a benchmark index comprising United States Government treasury notes, the Banking and Payments Authority has invested the assets of the Petroleum Fund in such notes, which carry the highest credit rating. The maximum loss that the Petroleum Fund would suffer as a result of a default by the United States Government is the value disclosed in the Balance sheet.

(b) Concentration of Credit Exposure

The Petroleum Fund’s significant end-of-year concentrations of credit exposure by the industry of the issuer were as follows:

Sovereign Issuers:	US Dollars
- United States Government	\$649,348,945

(c) Credit Exposure by Credit Rating

The following table presents the Petroleum Fund’s balance sheet classified according to the Standard and Poor’s credit rating of the issuer. AAA is the highest rating possible and indicate that the entity has an extremely strong capacity to pay interest and principal. AA is a high grade rating, indicating a very strong capacity, and A is an upper medium grade, indicating a strong capacity to pay interest and principal. BBB is the lowest investment grade rating, indicating a medium capacity to pay interest and principal. Ratings lower than AAA can be modified by + or – signs to indicate relative standing within the major categories.

	US Dollars	
	Balance Sheet	AAA
FINANCIAL ASSETS		
Cash and cash equivalents	499,284	499,284
Interest receivable	3,215,759	3,215,759
Receivables from pending sales of investments	-	-
Investments at fair value through profit or loss	646,133,185	646,133,185
Total Assets	649,848,228	649,848,228

(d) Credit Exposure by Counterparty as a percentage of the Petroleum Fund’s Capital

The assets of the Fund exposed to the United States Government amounted to 100% of the Petroleum Fund’s capital.

15. Interest Rate Risk

Interest rate risk is the risk of loss arising from a change in interest rates.

The Petroleum Fund manages this risk by investing passively according to well-defined industry benchmarks.

The assets and liabilities of the Petroleum Fund will re-price within the following periods:

	US Dollars					
	Balance Sheet	Non-interest sensitive	6 months or less	6 to 12 months	1 to 2 years	2 to 5 years
FINANCIAL ASSETS						
Cash and cash equivalents	499,284	-	499,284	-	-	-
Interest receivable	3,215,759	3,215,759	-	-	-	-
Investments at fair value through profit or loss	646,133,185	-	151,329,847	103,798,765	160,390,564	230,614,008
Total Assets	649,848,228	3,215,759	151,829,131	103,798,765	160,390,564	230,614,008
Weighted average interest rate		0.00%	4.38%	5.46%	3.52%	5.33%

16. Currency Risk

Currency risk is the risk of losses arising from changes in foreign exchange rates.

The Petroleum Fund is required by the Petroleum Fund law to manage this risk by investing in United States dollar denominated instruments, the United States dollar also being the official currency of Timor-Leste.

The assets of the Petroleum Fund in United States dollars are exactly matched by its liabilities, as set out in the following table:

	Balance Sheet	Currency of denomination : US Dollars
FINANCIAL ASSETS		
Cash and cash equivalents	499,284	499,284
Interest receivable	3,215,759	3,215,759
Receivables from pending sales of investments	-	-
Investments at fair value through profit or loss	646,133,185	646,133,185
Total Assets	649,848,228	649,848,228
FINANCIAL LIABILITIES		
Payable for pending purchases of investments	-	-
Net Assets	649,848,228	649,848,228

17. Market Risk

(a) Liquidity risk

Liquidity risk is the risk that the Petroleum Fund will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity may result from an inability to sell a financial asset quickly at close to its fair value.

The Petroleum Fund manages this risk firstly by investing in instruments that do not give rise to commitments that may need to be met, and secondly by investing solely in United States Government Notes, for which a highly liquid and deep market exists.

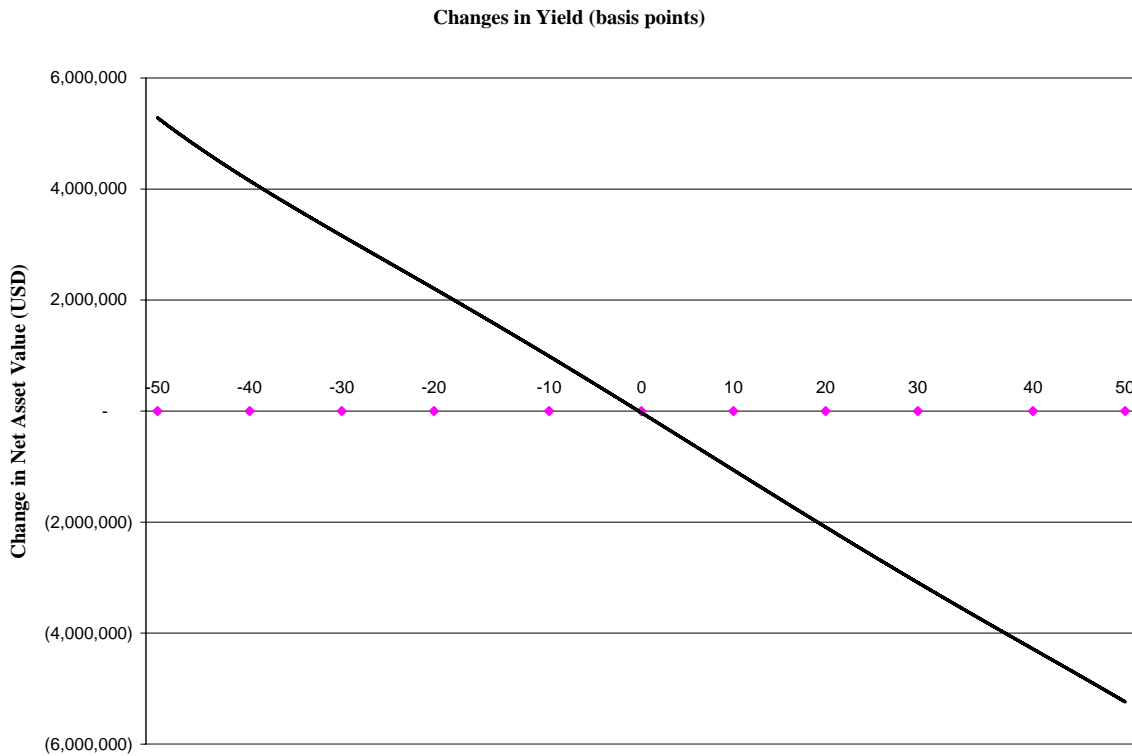
(b) Market risk

Market risk is the risk that the Petroleum Fund may encounter high market prices, giving low yields, at the point investments mature and the funds are available for reinvestment.

The Petroleum Fund manages its investment portfolio according to a passive investment mandate, and accordingly does not specifically manage this risk.

The principal tool used to manage and control market risk exposure is modified duration. As an approximation, the investment portfolio's modified duration can be used to calculate the change in the portfolio value for a given change in the interest rate. This is a good approximation when interest rates are small. If duration is used to measure the changes in prices for larger changes in interest-rate the estimation will be inaccurate due to the convexity effect, though the estimate will always overestimate the changes in net asset value.

The modified duration of the Petroleum Fund investment portfolio at 30 June 2006 was 1.70 years. The following graph shows a sensitivity analysis based on the assumption of a parallel shift in the yield curve between -50 and +50 basis points, where 100 basis points are the same as 1%.



18. Reconciliation of Net Cash Flows with Reported Operating Surplus

	US Dollars 2006
Reported Operating Profit	7,048,296
Add/(Subtract) Non-Cash Items	
Interest receivable	(3,215,759)
Net unrealised loss	<u>5,831,519</u>
Net cash flow from operating activities	<u>9,664,056</u>

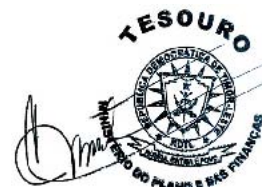


REPÚBLICA DEMOCRÁTICA DE TIMOR-LESTE
MINISTÉRIO DO PLANO E DAS FINANÇAS
GABINETE DA TESOURO

To : Sr. Cristino Gusmao, Macroeconomic Unit, MoPF

Cc: Sra. Aicha Bassarewan, Vice-Ministra do Plano e das Finanças

From : Sr. Manuel Monteiro, Deputy Director Treasury, MoPF



Díli, 29 de Dezembro 2006
Ofício N.º 81 / XII / 2006

Subject: Statement on accounting policy for Petroleum Fund

With respect to the provisions of the Article 24.1 part (c) of the Petroleum Fund Law, following statement on the accounting policy may be kept for your record:

“In accordance with Article 21 of the Petroleum Fund Law, the Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS) which comprise standards and interpretations approved by the International Accounting Standards Board (IASB) and International Accounting Standards and Standing Interpretations Committee interpretations approved by the International Accounting Standards Committee (IASC) that remained in effect at the Petroleum Fund’s balance date. The Financial Statements of the Petroleum Fund have also adopted *IFRS 7: Financial Instruments Disclosures* although the effective date for the standard is 1 January 2007.”

Best Regards

Statement of comparison of income with last three years***(As per Article 24.1 (d) of Petroleum Fund Law No. 9/2005)***

Financial Year 2005-06 is the first year of operation of the Petroleum Fund, therefore no comparison for previous three years can be given. However the income for the current is shown below. Please refer to the Income Statement of the Financial Statements for details.

(US Dollars)

FY 2005-06	FY 2004-05	FY 2003-04	FY 2002-2003
7,048,296	Not Applicable	Not Applicable	Not Applicable

Statement of comparison of nominal income on the investment of Petroleum Fund assets with the real returns after adjusting for inflation

(As per Article 24.1 (e) of Petroleum Fund Law No. 9/2005)

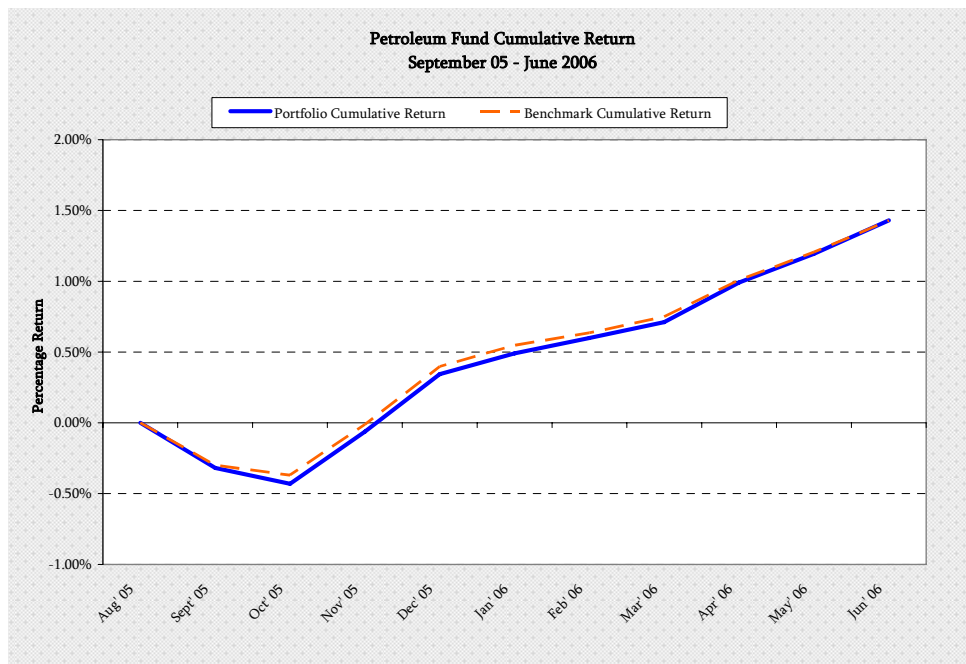
Financial Year 2005-06 is the first year of operation of the Petroleum Fund, therefore no comparison for previous three years can be given. However comparison of nominal income on the investment of Petroleum Fund assets with the real returns after adjusting for inflation is given below.

The average yield to maturity of the investments made through the period 9 September 2005 through 30 June 2006 has been estimated at 4.64 percent. During the period from September 2005 to June 2006 inflation in US was 3.2 percent, the real return on the investments, based on the yield to maturity, is accordingly 1.4 percent.

Statement of comparison of income on the investment of Petroleum Fund assets with the benchmark performance indices

(As per Article 24.1 (f) of Petroleum Fund Law No. 9/2005)

Statement of comparison of income on the investment of Petroleum Fund assets with the benchmark performance indices is given below.



PERFORMANCE SINCE INCEPTION

YTD Performance 2005/2006

	Portfolio	Benchmark	Excess return	Cumulative Portfolio	Cumulative Benchmark
Aug' 05	0.00%	0.00%	0.00%	0.00%	0.00%
Sept' 05	-0.32%	-0.30%	-0.02%	-0.32%	-0.30%
Oct' 05	-0.11%	-0.07%	-0.04%	-0.43%	-0.37%
Nov' 05	0.37%	0.36%	0.01%	-0.06%	-0.01%
Dec' 05	0.41%	0.41%	0.00%	0.34%	0.40%
Jan' 06	0.15%	0.15%	0.00%	0.49%	0.55%
Feb' 06	0.11%	0.09%	0.02%	0.60%	0.64%
Mar' 06	0.11%	0.11%	0.00%	0.71%	0.75%
Apr' 06	0.28%	0.26%	0.02%	0.99%	1.01%
May' 06	0.20%	0.19%	0.01%	1.19%	1.21%
Jun' 06	0.23%	0.22%	0.01%	1.43%	1.43%
YTD	1.43%	1.43%	0.00%		

**Statement of comparison of Estimated Sustainable
Income for the Fiscal Year with the sum of transfers
from the Petroleum Fund for the year**

(As per Article 24.1 (g) of Petroleum Fund Law No. 9/2005)

Fiscal Year 2005-06 was the first year of operation of the Petroleum Fund and there was no Estimated Sustainable Income for the fiscal year. There was also no transfers from the Petroleum Fund during the year.

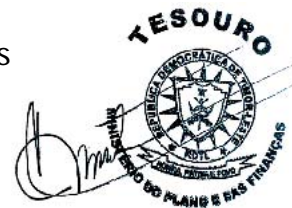


**REPÚBLICA DEMOCRÁTICA DE TIMOR-LESTE
MINISTÉRIO DO PLANO E DAS FINANÇAS
GABINETE DA TESOIRO**

To : Sr. Cristino Gusmao, Macroeconomic Unit,

Cc: Sra. Aicha Bassarewan, Vice-Ministra do Plano e das Finanças

From : Sr. Manuel Monteiro, Deputy Director Treasury, MoPF



Díli, 29 de Dezembro 2006
Ofício n.º 80 / XII /2006

Subject: Borrowings during the FY 2005-06

During the Fiscal Year 2005-06, there were no borrowings by the Government.

This may kindly be kept for record as required under the Petroleum Fund Law no 9/2005.

Best Regards

List of persons holding relevant positions for the operation and performance of the Petroleum Fund

(As per Article 24.1 (i) of Petroleum Fund Law No. 9/2005)

The list of persons holding relevant positions for the operation and performance of the Petroleum Fund is given below

- (i) Minister of Planning & Finance

Maria Madalena Brites Boavida

- (ii) Director of Treasury

Maria Madalena Brites Boavida

- (iii) Members of Investment Advisory Board

SI No.	Name	Position
1.	Abrão Fernandes de Vasconcelos	Director General of Banking & Payments Authority of Timor-Leste
2.	Cristino Gusmao	Coord. of Macro Economic & Tax Policy
3.	Sigurd Klakeg	Advisor of Fiscal Policy & Petroleum Fund
4.	Manuel Monteiro	Director of National Directorate of Treasury Substitution
5.	Torres Trovik	Advisor of Petroleum Fund

- (iv) External Investment Manager

Not appointed

- (v) Administrator of the Central Bank

Abrão Fernandes de Vasconcelos

Director General of Banking & Payments Authority of Timor-Leste

- (vi) The Consultative Council for Petroleum Fund was not formally constituted till 30 of June 2006

Compilation Report to the Ministry of Planning and Finance, Democratic Republic of Timor-Leste in respect of the Statement of Petroleum Fund Receipts for the year ended 30 June 2006

On the basis of information provided by management we have compiled, in accordance with the International Standard on Related Services applicable to compilation engagements, the Statement of Petroleum, Fund Receipts (the 'Statement') for the year ended 30 June 2006.

This special purpose report has been prepared in accordance with the requirements of Article 35 of the Petroleum Fund Law listing all payments made to the Petroleum Fund by payer. The Government, as represented by the Minister for Planning and Finance is responsible for the Statement.

DELOITTE TOUCHE TOHMATSU



Jody Burton
Partner
Chartered Accountants
Darwin, 23 April 2007

Petroleum Fund of Timor-Leste
Statement of Petroleum Fund Receipts
for the period 1 July 2005 to 30 June 2006

Payee	Receipt (USD\$)
Article 6.1 (a) Receipts	800
Advanced well Technologies Pty Ltd	
Amec Engineering Pty Ltd	196,556
Australian Int. Petro-Consultant Pty Ltd	20,485
Baker Hughes Australia Pty Ltd	1,115,161
Bawana Margatama Pty Ltd	144,534
BJ Process And Pipeline Service	169,848
BJ Services Company Australia	2,351
Brunel Energy P/L	68,155
Cameron Australia Pty Ltd	11,597
Coates Hire Operations P/L.	219,851
Code Engineering Services Pty Ltd	337,798
Compass Group (Australia) Pty Ltd	51,195
Conoco Philips JPDA Pty Ltd	9,040,745
Conoco Phillips (03-12) Pty Ltd	161,460,574
Conoco Phillips (03-13) Pty Ltd	14,958,921
Conoco Phillips (03-19) Pty Ltd	10,614,925
Conoco Phillips Australia Pty Ltd	21,107,916
Elang EPS PTE LTD	20,880
Emet Pty Ltd	511,086
Engineering Services Pty Ltd	5,707
Eni JPDA 03-13 Ltd	37,009,790
Ensko International Inc.	275
Expro group Australia Pty Ltd	41,059
Furmanite Australia P/L	29,580
Geographe Energy	62,819
Halliburton Australia Pty Ltd	646,226
Honeywell Ltd	47,569
Inpex Shaul Ltd	30,477,078
Intico WA Pty Ltd	64,480
Link Project Services P/L	25,967
Lloyd Helicopters Pty Ltd	246,537
Mentor Int. Mgnt Consultant Ltd	717
Monsoon Maritime Services Pty Ltd	32,196
Optima Solutions UK Ltd	76,126
Pae Singapore Pty Ltd	17,570
Petroz (Timor Sea) Pty Ltd	3,948,502
ProSafe Personnel Pty Ltd	65,635
PT Sillo Bahari Nusantara	158,983
Roxar Pty Ltd	9,518
Santos Ltd.	39,465,321
Saybolt Australia PL	46,069
SGS Australia Pty Ltd	111,989
Skilled Group Ltd	4,838
Solar Turbines Services Pty.Ltd.	8,716
Tad/Adecco Pty Ltd	66,353
Tenix Defence System Pty Ltd	20,464
Tidewater Marine Australia Pty Ltd	127,086
Timor Sea Designated Authority	93,126

Payee	Receipt (USD\$)
Tokyo Timor Sea Resources PIL	25,016,340
Total Marine Services Pty	121,865
Transworld Skill Services	15,843
Veritas DGC Australia Pty Ltd	15,057
Weatherford Australia Pty Ltd	7,119
Woodside Petroleum (Timor Sea) Pty Ltd	663,836
	358,803,735
Other Revenue	
BGP Inc.	1,695,743
ENI Australia Ltd	125,000
Petronas	50,000
Reliance Industries Ltd	50,000
	1,920,743
Total receipts from Article 6.1 (a)	360,724,478
Article 6.1 (b) Receipts	
Timor Sea Designated Authority	77,471,749
Total receipts from Article 6.1 (b)	77,471,749
Article 6.1 (c) Receipts	
Interest received	9,934,056
Total receipts from Article 6.1 (c)	9,934,056
Total Petroleum Fund Receipts	448,130,283

Compilation Report to the Ministry of Planning and Finance, Democratic Republic of Timor-Leste in respect of the Extractive Industries Transparency Initiative Return for the year ended 30 June 2006

On the basis of information provided by management we have compiled, in accordance with the International Standard on Related Services applicable to compilation engagements, the accompanying Extractive Industries Transparency Initiative Return (“the Return”) of the Government of Timor-Leste for the year ended 30 June 2006.

This special purpose report has been prepared in accordance with the Reporting Guidelines of the Extractive Industries Transparency Initiative for the purpose of disclosure in the Reporting Template of the Government of Timor-Leste. The Government, as represented by the Minister for Planning and Finance is responsible for the preparation of the Return.

DELOITTE TOUCHE TOHMATSU



Jody Burton
Partner
Chartered Accountants
Darwin, 23 April 2007

A Input template for Host Government Reporting Entity

Host Country reporting on: Petroleum Fund of the Democratic Republic of Timor Leste

Reporting Period: 1 July 2005 to 30 June 2006

Scope 1 Benefit Streams

Line ref	Guidelines section 6 ref	Volume	Value SUSD
1	Benefit Stream from International Companies only		
1a)	Host Government Production Entitlement from International Companies	i	
	i) Production Stream – in kind		
	*[specify nature of production and units]	N/A	-
	*[specify nature of production and units]	N/A	-
	ii) Production Stream – in cash		-
2	Benefit Stream from National State-Owned Companies		
2a)	Host Government Production Entitlement from National State-Owned Company	i	
	i) Production Stream – in kind		
	*[specify nature of production and units]	N/A	-
	*[specify nature of production and units]	N/A	-
	ii) Production Stream – in cash		-
3	Benefit Streams from International and National State-Owned Company		
3a)	Profit taxes	iii	358,803,735
3b)	Royalties	iv	
	- in cash		77,471,749
	- in kind		-
3c)	Dividends	v	-
3d)	Signing bonuses and production bonuses	vi	-
3e)	License fees, rental fees, entry fees and other considerations for licenses/concessions	vii	-
3f)	Other payments to Host Governments, specified as:	viii	
	<u>Bidding Fees</u>		225,000
	<u>Mapping Fees</u>		1,695,743
			-

Scope 2 Benefit Streams

Line ref		Volume	Value
4	Scope 2 Benefit Streams (voluntary disclosure):		
	N/A	N/A	N/A

Host Government sign off

We acknowledge our responsibility for the fair presentation of the Reporting Template in accordance with the Reporting Guidelines.

Basis of Preparation

This statement has been prepared in accordance with the Revised Draft Reporting Guidelines issued by the Extractive Industries Transparency Initiative on 23 May 2003. The reporting currency is the US dollar. Benefit Streams have been reported on the cash basis of accounting.