This PowerPoint presentation was used in an all-day budget workshop for Timorese NGOs in the Core Group Transparency and others on 8 July 2008.

The Ministry of Finance issued this press release in response to the first debate about cars for members of Parliament. That release categorically asserted that there were no plans to buy cars for every MP, an assertion which became false when the Council of Ministers approved the mid-year budget rectification the following day.

RDTL Constitution

Section 145 (State Budget)

1. The State Budget shall be prepared by the Government and approved by the National Parliament.
2. The Budget law shall provide, based on efficiency and effectiveness, a breakdown of the revenues and expenditures of the State, as well as preclude the existence of secret appropriations and funds.
3. The execution of the Budget shall be monitored by the High Administrative, Tax and Audit Court and by the National Parliament.

I. General Concepts

- **Receitas / receipts / rendimentu**
- **Despesas / expenditures / gasta**
- **Deficit** (gap between expenses and revenue)
- **Carryover** (money not spent in one budget year which is available for the future)
- **Sustentaveis / sustainable / sustentavel** (able to continue for the indefinite future)

There are apparently no Tetum words for deficit or carryover.

Categories of Expenditures

- Salaries (salarios e vencimentos)
- Goods and Services (bens e servicos)
- Minor Capital (capital menor)
- Capital Development (capital e desenvolvimento)
- Transfers (transfarencias publicas)

Good and services are supplies that are used up, consultants, contractors, etc.

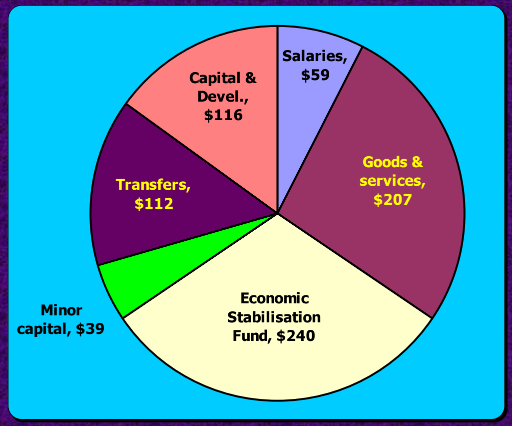
Minor capital is things like cars, computers, and furniture for government that lasts about five years.

Capital Development is buildings, major infrastructure, that lasts longer and supports the national economy.

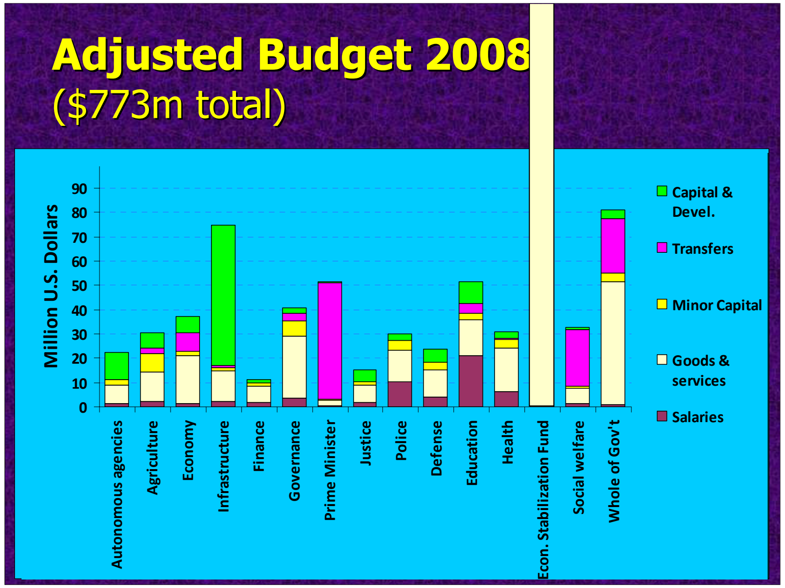
Budget Rectification training 7/25/2008

Mid-Year Adjusted Budget 2008

Total expenditures: USD $773.3 million



ESF is listed as goods and services in the budget documents, only for 2008. We separated it out to make it clearer.



Economic Stabilization Fund -- $240 million, higher than the entire national GDP during the period July-Dec 2008. For comparison, Timor-Leste's total volume of imports (excluding re-exports) is under $200 million per year.

Transfers:

PM originally $5m for church, $15m IDPs, $5m petitioners. MYBU added $20m more for IDPs, $3m for petitioners.

Whole of Gov't: $16m veterans, $540k former office-holders, MYBU added $4.5m veterans.

Social: Old age pension $6.1m, $2.5 children & vulnerable groups. MYBU added $10.8m for old age pensions.

Categories of Income

- **Domestic Taxes / Impostos Domesticas** (these will drop because of tax reform law)
- **User Fees / Taxas de Utilização** (mainly rice sales, and perhaps other sales)
- **Petroleum Fund ESI** (plus more)
- **Donor budgetary support** (ended already)
- **Donor projects** (not included in State Budget; *Combined Sources Budget* no longer used)

"Rice" sales may include construction materials and fuel, as they're not listed elsewhere in the budget.

Until this budget cycle, the Ministry of Finance also published a "Combined Sources Budget" which listed donor projects and assistance which was coordinated with the Government, as shown on the next slide. But for this mid-year update, the Ministry of Finance has not made such information available.

From original 2008 Budget
Combined Sources Financing

Table 2.2

Financing of the Combined Sources Budget 2006-07 to 2011 ($m)

	2006-07 Actual	2007 Estimate	2008 Estimate	2009 Estimate	2010 Estimate	2011 Estimate	Total 4 Years
Revenue	**59.3**	**115.5**	**181.7**	**140.8**	**102.0**	**144.3**	**568.8**
Domestic Revenue	40.9	14.4	20.7	20.1	20.8	76.0	137.6
Direct Budget Support	11.4	-	-	-	-	-	-
Autonomous Agency Revenue	7.0	2.5	6.3	6.5	6.7	22.0	41.6
Confirmed Donor Funding		98.5	154.7	114.2	74.5	46.3	389.7
Expenses	**161.9**	**213.4**	**502.5**	**397.2**	**346.8**	**325.1**	**1,571.5**
Recurrent Expenditure	150.2	201.9	428.5	347.7	314.9	294.2	1,385.3
State Budget Funding	*150.2*	*110.5*	*280.1*	*235.4*	*240.8*	*248.3*	*1,004.6*
Confirmed Donor Funding		*91.4*	*148.4*	*112.3*	*74.1*	*46.0*	*380.7*
Capital Expenditure	11.6	11.5	73.9	49.4	32.0	30.9	186.2
State Budget Funding	*11.6*	*4.4*	*67.6*	*47.5*	*31.6*	*30.6*	*177.3*
Confirmed Capital Funding		*7.1*	*6.3*	*1.9*	*0.4*	*0.3*	*9.0*
Expenses							
Transfer from the Petroleum Fund	102.5	40.0	294.0	256.3	244.9	214.7	1,009.9
Existing Cash Reserves	-	(57.9)	(26.8)	-	-	-	(26.8)

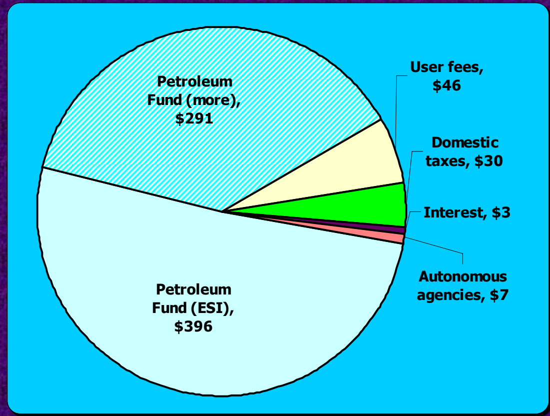
This is last December's Combined Sources Budget; the Government did not produce one for the Rectification.

Gov't omitted donor funding for 2006-7, but there was some.

2007 is only six months.

Direct Budget Support used to come from Portugal; but is not done any more?

Budget Adjustment 2008
Total revenues: USD $773.3 million



Domestic taxes will drop from $30 million in 2008 to about $18 million per year in future years, because of the new Tax Reform law. (The new tax reform law goes into effect on 1 January 2008 for annual taxes and 1 July 2008 for indirect taxes., but the MYBU does not assume it until 2009, as far as we can tell.)

Of the $30.3 million domestic taxes in 2008, $12.8 is business income ($9.5) and wage ($3.3) tax , and $17.5 is indirect tax, mostly import duties and excise tax.

In past years, **user fees** have been less than $5 million/year. In 2008 and for the next four years, they are projected at about $50 million/year, almost all from selling rice. There is no other income listed from selling subsidized goods.

Autonomous Agencies
Agências Autônomas

These can be included, or not

- TL Electricity Department
- Nicolau Lobato Airport
- APORTIL, including Dili port and Nakroma ferry
- Equipment Management Institute

Receipts = Expenses
$22 million in 2008

The new National Petroleum Authority (ANP/NPA) is not included, even for future years. It appears to be funded totally off-budget, except for an initial $1.249 million to establish it this year.

Timor-Leste changes every year

- **Population increases**
  3.5% per year, will double in twenty years.
- **Inflation / prices go up**
  IMF expects 9.0% in 2008, 5-7% in next three years.

Therefore, the cost of providing the same services increases 13% every year.

See IMF document on LH MYBU web page at http://www.laohamutuk.org/econ/MYBU08/IMFcr08202.pdf

Recurring and one-time expenses

- **Most expenses recur** every year, as most government services and salaries are ongoing.
- **Special one-time expenses** – IDP resettlement and money for petitioners.
- **Development capital costs** – buildings, big infrastructure, last for decades
- **Minor capital** – cars, computers – last about 5 years
- **Multi-Annual projects** are approved now and spent over several years. Can be any category.

This is important to understand when projecting the impact of the budget into the future.

The ESF is budgeted as a one-time cost, but is this realistic? Other countries have experienced civil unrest when they try to reduce or end subsidies.

Budget Execution

- Ongoing problem in TL
- Big plans, low capacity to implement them.
- AMP is obsessed with this, hence using funds and transfers, which are easier.
- Reports are misleading, as commitments and obligations are counted as executed.
- Carry-over from past years has paid for all gov't activities during the first half of 2008.

TL will be better off if the 2008 mid-year budget is not executed – if it is the following years will require borrowing.

Budget execution is only a measure of spending money, not whether anything useful is done with the money. Program performance is much more meaningful. It's quite possible to spend (or lose) a lot of money without any benefit for the people.

Budget Execution

Transitional 2007 Budget (Jul-Dec 2007)

	Appropriation		Actual Expenditure			
	Original	Revised	Cash Payments		Total Expenditure	
Salary & Wages	19,485	19,603	17,442	89%	17,442	89%
Goods & Services	73,107	68,403	37,116	54%	59,837	87%
Minor Capital	2,964	5,624	688	12%	5,286	94%
Capital & Development	8,739	10,665	727	7%	10,575	99%
Transfers	12,114	12,114	8,363	69%	11,731	97%
Total	**116,409**	**116,409**	**64,336**	**55%**	**104,871**	**90%**

Fruit for executioners! Is it better to be a banana or a durian?

Note that cash payments are much less than total expenditures. The “total” includes commitments and obligations – that is, contracts which have been signed but not yet carried out. Many of these never happen, and are never paid for. And the ones which are could be counted twice – once as commitments, and a second time as cash. So “Cash Payments” is the only meaningful measure of execution, as that’s the only indication that the actual government activity took place. After all, the gov’t’s function is not to spend money, but to provide services.

II. How to read the budget

- Look at each section of the documents
- Find the information that you need
- If it’s not there, use other sources or estimate

Introduction to next session

Parts of the budget document

1. Executive summary, p.4
2. Explanation of motives from the PM, separate
3. Fiscal and economic overview, p.6
   Petroleum Fund: Chart/table 3.4
4. Revenues (domestic), p.22p/21e
5. Expenses, p.25/24
   Execution, revision
6. Chart 5.6, p.31/29, The cost of each new program

The first page number is the Portuguese version, the second in English. Only the English is on LH’s website http://www.laohamutuk.org/econ/MYBU08/MYBUDocEn.pdf; Portuguese only available on paper so far.

An annotated version of the English budget document goes with this PowerPoint, at http://www.laohamutuk.org/econ/MYBU08/AnnotatedBudgetDocument.pdf, with comments on particular items.

7. Information about each ministry. p43/35
8. Annex 1&2: expenditures in original and revised budgets, by category. p129/106.
9. Annex 3: breakdown of 2008 expenditures by organ and category. p120/108. This table is also Annex II of the budget law.
10. Annex 4: capital plan 2008-2011. Includes original and revised budget expenditures, by year. P 148/125
11. Annex 5: staffing profile. p170/147

12. Annex 6: budget law. p.separate/162. This is the law that Parliament must pass.
13. Annexes to Budget law (part of the law)
    I. Revenue estimates
    II. List of expenditures (same as Annex 3 of budget document)
    III. Autonomous agencies
    IV. Multi-year capital projects
14. Annex 7: subsidies for autonomous agencies. P198/168
15. Annex 7(sic): report from independent auditor about petroleum fund. P199/169

III. Important issues

- Size and implementation of Economic Stabilization Fund
- Overspending the Petroleum Fund
- Multi-year projects
- 2009-2011 budget deficits
- Public consultation and access to information
- Capacities of Government and Parliament

Introduction to next session

Economic Stabilization Fund

- $240 million, new in MYBU, only for 2008
- Very little information available, so we have to make educated guesses
- To subsidize
  - Rice – security of food supply
  - Stabilize fuel and other commodity prices
  - Construction materials – encourage development and private investment
- How long will the subsidies continue?

One subsidies start, they are very hard to stop.

Government budgets to receive $39.4 million this year from selling rice, and $49.4m/year over the next three years; how does this relate to ESF?

The Government has also added $4.6 million to the Whole of Government expense budget for "taxes on rice imports" to cover the

Government's legal obligation to pay tax when it imports rice and other commodities."

Tibor will estimate the amount of rice.

The money all goes overseas, to pay for imports, and do nothing to develop the local economy.

Total imports of everything to TL are now about $200 m/year, so ESF is larger than all other imports put together.

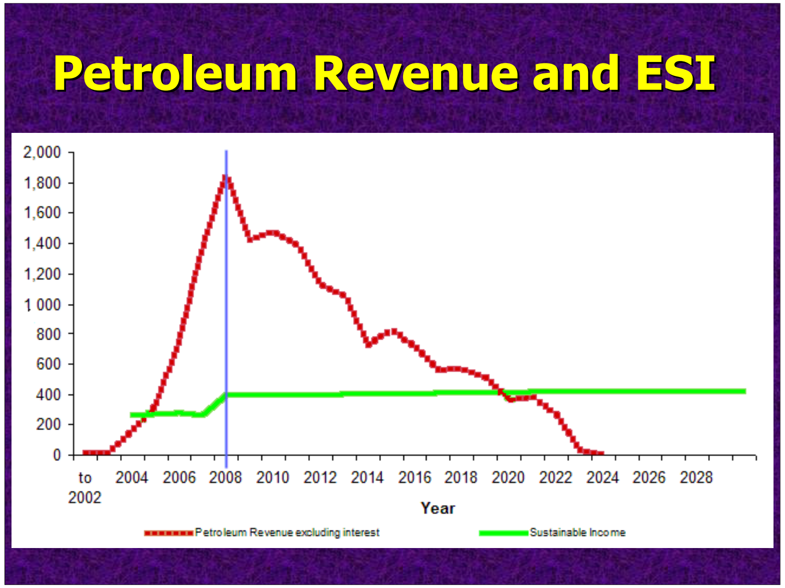
In addition to hurting local agriculture in the short term, it will change people's buying habits and hurt food security in the long term.

See also Core Group analysis of ESF, at http://www.laohamutuk.org/econ/MYBU08/CGT-ESF23Jul08En.pdf

Petroleum Fund objectives

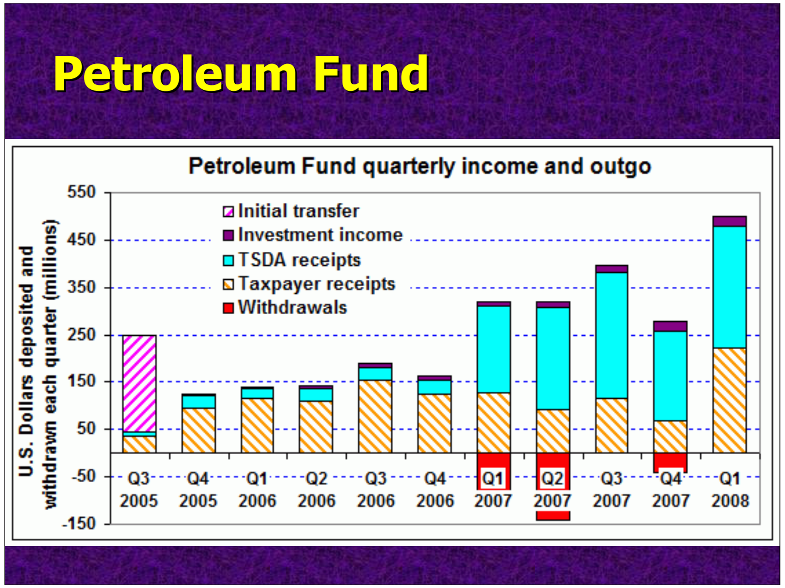
- Smooth out gov't revenues when oil prices fluctuate
- Provide sustainability after petroleum is exhausted, in about 15 years (unless Sunrise is developed)
- Reduce temptation to over-spend when oil revenues are high

Constant inflation-corrected dollar income from ESI isn't "sustainable" when TL's population doubles every 20 years.

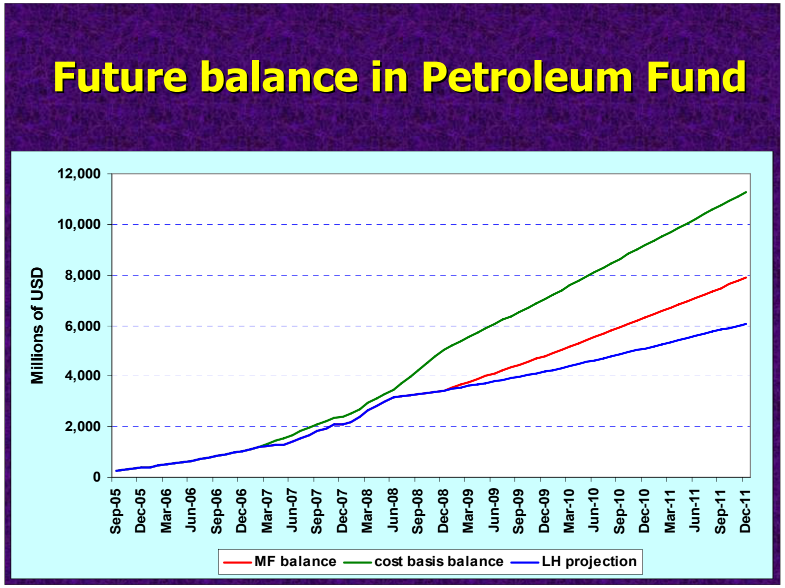


Blue vertical line is today. Note that we are at the peak of oil income, and that production from Bayu-Undan will decline pretty rapidly as the field is used up. Income will be less than half of current levels in just five years!

The step in ESI (green line) just before now is the gov't re-calculation based on higher assumed oil prices. But there's no reason to expect them to stay as high as they were in late June.



History of deposits and withdrawals in Petroleum Fund. There have not been any withdrawals so far in 2008. At the end of June, the balance was $3,203,073,000.



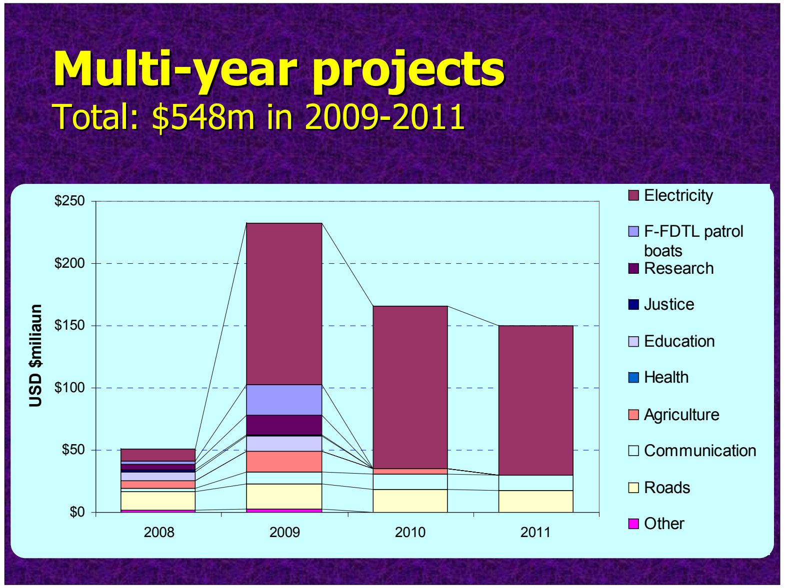
Green line is what the monthly balance in the PF would be if no money was withdrawn, just looking over the next three years.

Red is balance if gov't keeps to plan to go over ESI in this year only,

Blue is LH's projection that gov't will have to go over ESI every year, even more than this year.

Assumes 5% interest, **not** correcting for inflation.

Taking $291 million above the ESI this year alone reduces the future ESI by about $9 million each year. After 32 years, TL will have lost more money than it gained from going over this year, and will continue to pay "debt service" of $9 million each year forever.

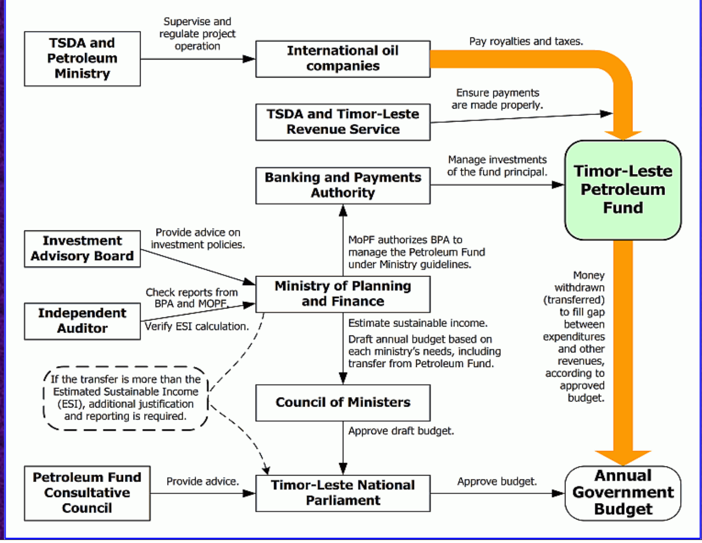


This is a new feature of this budget. The biggest one is the electric generating plant, but several others are front-loaded, so that they look like lower costs in 2008, but more in future years. This will make the 2009 budget at least $100 million more than the 2008 one.

If the ESF subsidy is not drastically reduced, that will be about $480 million (over 12 months) in 2009, up from $240 for the last six months of 2008.

This would make the total 2009 budget over a BILLION dollars – see later scenarios.

Figure 4: Agencies involved with Timor-Leste's Petroleum Fund



This is the decision-making process for withdrawing money from the Petroleum Fund.

It should normally be done only once each year, but the major "rectification" has caused an extra cycle, as did the shift of fiscal year in 2007.

The new Government has been in office less than a year, and is in its third budget cycle!

Scenarios for 2009-11 budgets

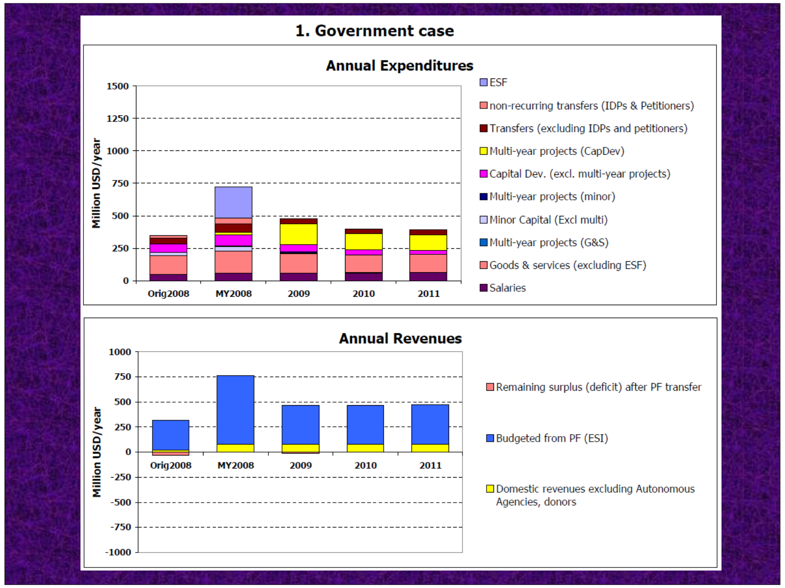
1. Government figures – not realistic
2. Constant expenditures, subsidies stop
3. Subsidies phased out, plausible expenses
4. Subsidies and other expenses continue, adjusted for inflation

All these scenarios use government assumptions for oil prices, revenues, multi-year projects, non-recurring costs, 2008 budget. None include carry-over.

The following four scenarios all use Gov't figures for multi-year and non-recurring expenses, oil prices, revenues, and future ESI (while assuming that deficits are filled from the PF) but make better projections for other items.

The first two assume that the subsidies paid for by the Economic Stabilization Fund end after 2008, an impractical idea, incorporated in the gov't budget, that could lead to social unrest.

1. Information exactly as in Government budget document. No minor capital, G&S, capital development and transfers decline sharply after 2008.
2. Adds reasonable assumptions for salary hikes, minor capital (constant) G&S (constant), capital Dev. (const. at lower level than 2008), transfers (const. at lower level).
3. Same as #2 with inflation added to G&S and transfers. Capital constant at higher levels. ESF phased out: 360, 300, 240 per year. Under this scenario, the ESI is $51 million per year less than it would have been if it had never been violated.
4. Same as #3 with inflation and growing population calculated for capital development, transfers similar to 2008 (inflation corrected, but excluding IDPs and petitioners), ESF at $480m/year corrected for inflation and population. In this case, the ESI will have been reduced by $81 million per year forever, even if it is never exceeded again.



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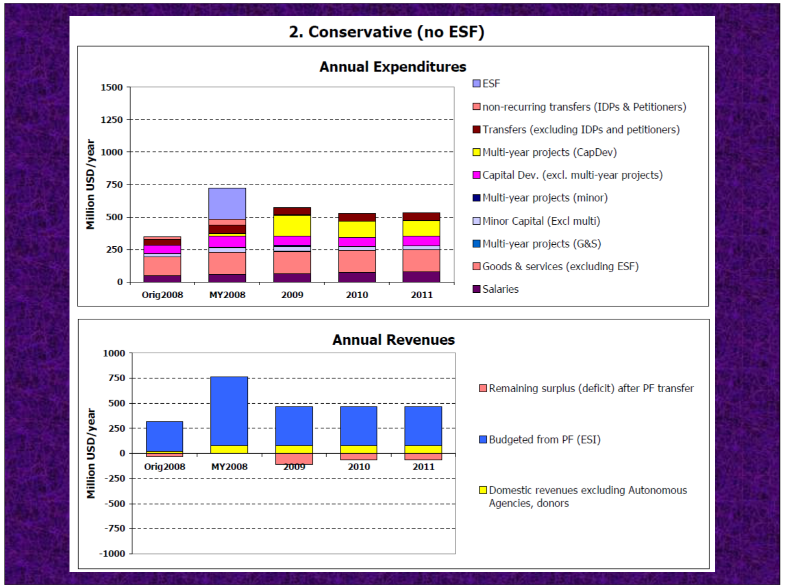

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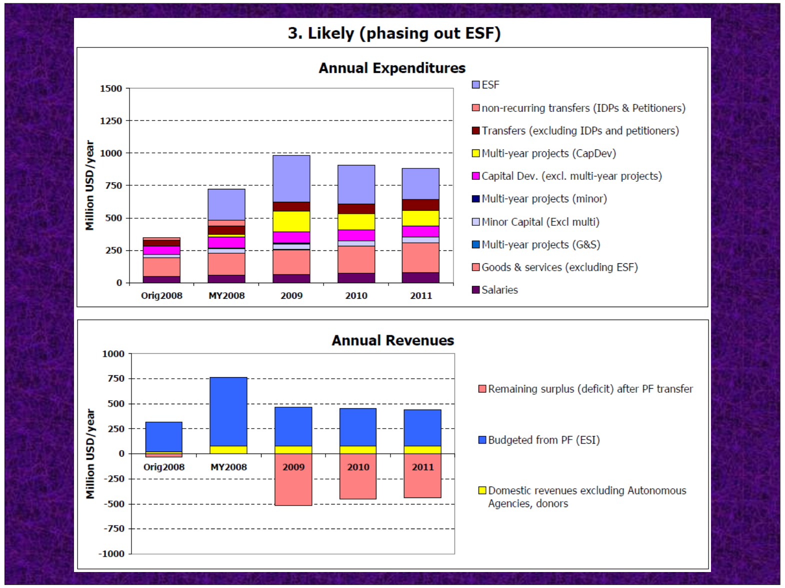

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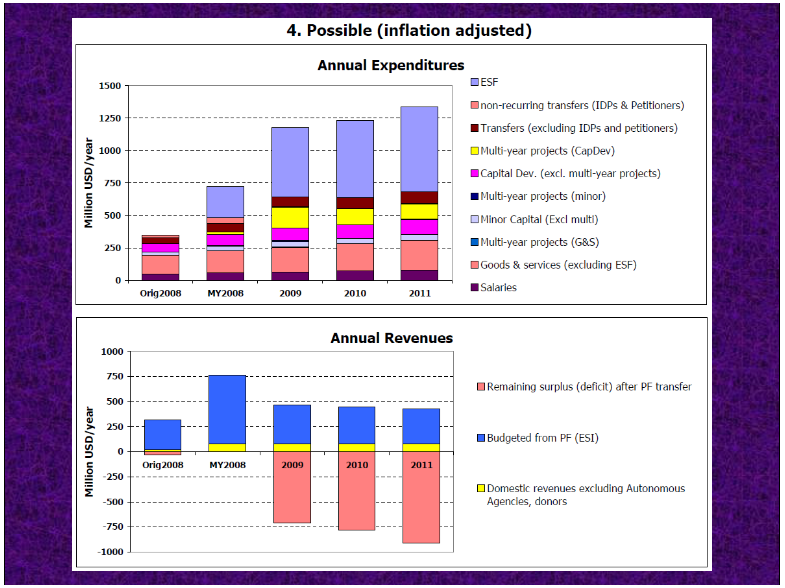

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