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Submission to
Committee C, National Parliament of Timor-Leste

From
La'o Hamutuk

Regarding
The Proposed General State Budget for 2021

13 November 2020

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Introduction

Firstly, La'o Hamutuk expresses its appreciation to the Parliament's initiative in organising the two-day "Panorama Orsamentál" seminar, and for inviting civil society, including La'o Hamutuk, to participate. We are also grateful to Committee C of the National Parliament, which gave us the opportunity to share our thoughts about the presentations made at the Panorama.

Since the Panorama had limited time, we would like to share our analysis, critical thoughts, and suggestions through this submission to help Deputies in the National Parliament. We are disappointed that the hearings on the proposed 2021 General State Budget will not give an opportunity to civil society organizations, including La'o Hamutuk, to discuss alternative perspectives on the proposed budget that the Government has prepared.

Through this submission we wish to share our analysis and key recommendations regarding the proposed 2021 State Budget and allocations to key sectors. We hope that our ideas will be considered in the debate on the proposed 2021 State Budget.

The Government made its first withdrawal from the Petroleum Fund in March 2007. The Fund, through the returns on its investments, is the principal source of financing for the Budget. Every year the Government makes large withdrawals for the General State Budget. These transfers are regulated by law, and need to be explained in detail to Parliament when they exceed the Estimated Sustainable Income (ESI).

Since 2008, the transfer has always exceeded the ESI, which impacts the sustainability of the Petroleum Fund, and it seems perhaps this guideline is no longer relevant to the Government's policy orientation. However, these transfers continue to fund activities that are unsustainable, because experience shows that most of these transfers are eaten up by ever-increasing recurrent spending and by major projects that have not been realistically analysed and which fail to respond to the urgent conditions facing the Timorese people.

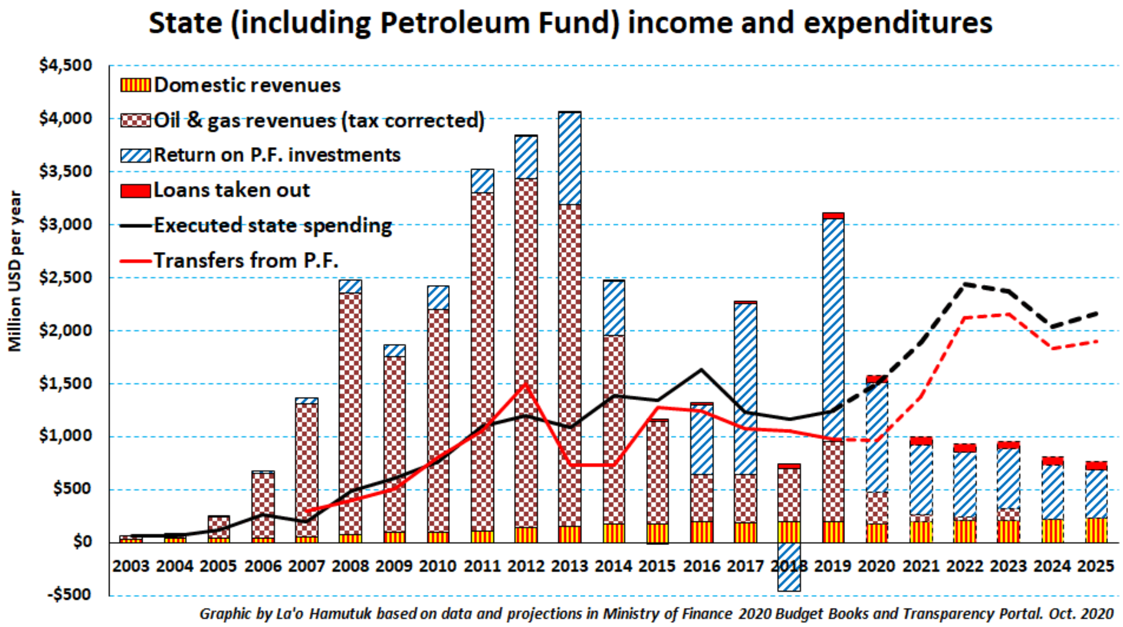
This situation is reflected in the Ministry of Agriculture's 2019 report, which shows that the nation's production levels remain low. Results of analysis by relevant agencies shows that we are yet to maximize food diversification, which results in a food insecurity rate of 36%, high levels of malnutrition particularly among children, and a multidimensional poverty rate of 46%.

We appreciate that the Government has started some initiatives and programs to invest in productive economic sectors, including some of the steps outlined in the Economic Recovery Plan such as the Basic Basket *(Cesta Bázika)* and plans to invest in agriculture through investment in cooperatives, in processing industries and other important sectors as a base to strength the economy within the country.

We therefore continue to encourage members of National Parliament to make good use of their responsibilities to analyze and discuss priorities with the Government, focusing attention on basic priorities related to the lives and economies of the people, to guarantee a sustainable well-being for our people today and for generations to come.

How Can We Guarantee the Sustainability of State Finances?

The Government of Timor-Leste currently faces a critical situation regarding the future of our oil and gas reserves, which projections show will be exhausted in the near future.



The above graph shows the difference between annual state income and state spending, including Petroleum Fund transfers and projections of the returns that the State will receive in the future.

Numbers from the Fund's managers and today's fiscal policies have consequences for the future. Timor-Leste is not using the petroleum money allocated through the State Budget with care to develop and promote economic diversification to non-petroleum activities. State spending depends greatly on the Petroleum Fund, but levels of spending exceed returns on investment, and so our Fund will be rapidly depleted. This critical situation is exacerbated by the Covid-19 pandemic, which has impacted the global economy, including investment values in global markets; oil prices, returns on stocks, and bonds all continue to fluctuate.

Despite ANPM's announcement that they have approved the proposal from Santos, as the new operator of the Bayu Undan field, to drill three new wells at the site to increase access to the remaining reserves, the likely revenues from these three wells will not last more than a year. The Government maintains high hopes of onshore and offshore drilling at Buffalo and other fields, but needs to recognize that revenues from these fields will be much less than those already received from Bayu-Undan. Given this situation, the Government of Timor-Leste needs to carefully manage its spending, and not prioritize sectors that require high spending but have not provided any benefit to the people of Timor-Leste or helped Timor-Leste develop sustainable revenue sources.

During two decades of independence, the Government has spent $12 billion from the Petroleum Fund to further unsustainable policy ambitions; the reality is that the people's economy has not yet developed in such a way that can provide for their long-term welfare, as was promised by the National Strategic Development Plan. To date, these dreams have yet to be realized because the Government has shown no commitment to invest in and develop productive economic sectors to diversify the economy and thus strengthen the people's economy in a way that will be sustainable when the Petroleum Fund has been depleted.

Principal Paths Forward for Timor-Leste's Government

The situation described above does not mean it is difficult for Timor-Leste to change, but with wise policies we can avoid future dangers.

At the moment, the Petroleum Fund contains $18.4 billion; the Government needs to find a way to increase other financing, especially from the local economy, including grassroots and other domestic economies. It's no secret that most of the money transferred from the Petroleum Fund by the Government have been to finance major projects that are now in doubt.

To avoid continuing to throw money away, the Government should conduct an independent and realistic study and analysis of the costs and benefits of planned future projects. The Government must also avoid programs that threaten the sustainability of the Petroleum Fund.

La'o Hamutuk continues to suggest that the Government invest in the people through education and health, which are important pillars to ensure a smart, innovative, and healthy population. Many nations without extractive industries are able to achieve strong economies because they prioritize the development of human resources. With the unique and limited wealth of the Petroleum Fund, Timor-Leste must choose this option to guarantee the people's welfare in the long term.

The Tasi Mane Project - Will it be Good for Timor-Leste's People?

We need an independent analysis of its costs, risks, and benefits to the people of Timor-Leste.

Aside from large transfers to state administration, the Government also continues to promote projects whose risks, benefits and costs have not been seriously analysed.

Based on Book 3A of the proposed 2021 General State Budget, the Government will allocate funds to compensate communities to be evicted to make way for elements of the Tasi Mane Project, including the second phase of the highway, refinery, Suai Supply Base, and LNG plant. In reality, the project itself is in doubt, and so we suggest that the Government not proceed with evicting local people from their homes and forcing them to sacrifice their productive lands and destroy other aspects of cultural, social, and economic significance where they live.

We appreciate that the Ministry of Petroleum and Mining has said it will re-evaluate the project, but we are confused by the Government's decision to continue allocating large amounts to related institutions, such as TimorGAP which is set to receive $71 million in 2021, when this re-evaluation is yet to occur. This indicates that the Government is thinking of continuing to promote these major projects.

Money spent, budgeted and required to build the Tasi Mane project (millions of USD)

Component	Location	Status	Spent through 2019	Budgeted 2020	Budgeted 2021	Budgeted 2022-2025	Estimated total capital cost	Percent budgeted
Airport	Suai	Constructed	75	3	3	9	100	91%
Supply base	Suai	Tender pending	51	1	5	745	900	89%
Highway	Suai-Fatukai	Mostly built	305	1	3	4	340	92%
Highway	Fatukai-Beaçu	Not started	3	0	1	22	1,320	2%
Airport	Viqueque	Not started	-	-	-	-	75	0%
Oil refinery & pipelines	Betano	Pending design	5	-	-	6	1,500	1%
Gas pipeline, LNG plant & port	Sunrise-Beaçu	Pending design, seeking financing	18	-	-	21	6,000	1%
57% share of Greater Sunrise Joint Venture	Offshore	Borrowed directly from the Petroleum Fund	650				650	100%
Interest on loan to buy into Sunrise JV	Offshore	Debt accrued in Petroleum Fund	21	30	32	141	512	44%
57% of Sunrise upstream capital expenditure	Offshore	Pending design, seeking financing	-	-		-	6,840	0%
Administrative and other costs	Dili	Ongoing	46	14	68	-	500	26%
TOTAL			1,174	49	112	948	18,737	12%

Table by La'o Hamutuk from Ministry of Finance budget books, General State Accts, TimorGAP proposal, transparency portal and our estimates. October 2020

Timor-Leste has already spent more than $520 million on the Tasi Mane Project, and has borrowed $700 million. The Government needs to understand that it is not the petroleum industry that can strengthen the national economy, but rather investments in the people. In addition, investments in productive sectors such as agriculture, processing industries, tourism, and manufacturing including cooperatives, to strengthen the people's economy and ensure financial sustainability now and into the future.

The Petroleum Fund is Not for Underwriting Loans

The proposed 2021 General State Budget provides information about the proposed new debt ceiling of $420 million, which would allow the Government to sign new loans up to of $400 million in 2021, and issue $20 million in public debt bonds. Before authorizing the Government to sign such large contracts and create debt for the next generation, Deputies and the public need access to complete information about the goals and impacts of future loans.

In relation to the objectives of the loans, although Figure 18 of Budget Book 1 shows the sectors that will receive funds from loans, there is unfortunately no detail on the specific projects to be funded, nor the terms and conditions of the loans, including the total that Timor-Leste will have to repay in the future.

Furthermore, Figure 22 in Budget Book 1, on repayment of debt shows the total amounts to be repaid each year through 2022. However, when the Government signs new concessional loan contracts, 2022 will still be in grace period when the principal is not being repaid, although interest accrues. The Government's estimates do not show the amounts to be repaid over the long term, and there is no information about the impact on future fiscal sustainability. Deputies need to fully understand longer-term estimates and the impacts of new loans, and make a decision carefully.

As the Government acknowledges in Figure 2 of Book 1, the Petroleum Fund may be empty by 2030. Timor-Leste has not yet identified or developed sustainable economic sectors that can replace the extraction of oil and gas from Bayu Undan when it ceases production in 2022 or 2023.[1] The Government has not yet analysed (or published) information about Timor-Leste's capacity to repay our debt after the Petroleum Fund is empty. Timor-Leste's capacity to fund basic services such as health and education will be in danger in 2030 when the Petroleum Fund nears depletion; the Government itself recognizes that "spending will decrease dramatically by 92% in 2028-2030…to just $386 million" (Book 1, page 11). With these limitations on our economic resources, what will our capacity to repay these loans be?

We suggest that National Parliament not approve any new debt ceiling without more detailed information, to avoid major risks to the coming generations.

The New Budget Model Reduces Transparency

La'o Hamutuk agrees with the objectives behind the Unit for Planning, Monitoring and Evaluation's (UPMA) Program-Based Budget Model, to improve responsibility, efficiency, efficacy, and transparency through aligning annual plans and annual budgets. UPMA's presentation to the Budget Panorama in November 2020 stated that the advantages of the Model are "increasing transparency and allowing the public to conduct checks and balances." They also stated that this model can facilitate dialogue within Parliament, "…not only discussing percentages that have been executed, but also the results achieved through the executed budget." However, the reality is that the information published through this new model damages transparency and accountability.

The new system proposes to provide data about budget allocations and outcomes based in individual programs. UPMA provides as example from the Ministry of Health in their presentation, to demonstrate how this model can provide a complete range of information. In reality, this model shows that many ministries continue to supply inadequate information about their activities, financial management, and outcomes. La'o Hamutuk observes that the Model does not succeed in facilitating dialogue and monitoring in Parliament, and will make it more difficult for the public to access information.

One example is the Ministry of Public Works; the Program-Based Budget Model considers 'Financial Management' as a discrete program, and $207 million is allocated to it. From Budget Book 4A we learn that this amount includes $194 million in public transfers. There is no information about the specific amounts allocated to clean water, electricity, sanitation, or other programs. We are concerned about the lack of clarity of the category 'Financial Management'; the new format means we cannot access detailed information about individual activities.

We suggest that the Program-Based Budget Model should consider specific individual programs, rather than those defined in a general way that reduces accountability and transparency.

[1] Proposed 2021 State Budget Books, Budget Overview, English version, Page 37, Table 19, accessible at: http://www.laohamutuk.org/econ/OGE21/books/OJE21BB1-Oct2020en.pdf

Autonomous Institutions Do Not Need Special Transfers

Furthermore, we do not agree with Government's creation of autonomous institutions to reduce work which has long been done by Ministries. In the 2020 General State Budget the Government created eight autonomous institutions, and in the proposed 2021 General State Budget the Government proposes to create five more: the Agency for Promotion of Investment and Exports, the National Water and Sanitation Authority, the National Electricity Authority, the National Ambulance and Emergency Medical Service, and the General Inspectorate of Labor.

Moving these programs and activities from the Ministries and Secretaries of State to autonomous institutions means that the Ministries will no longer manage their activities. These new institutions receive transfers in a way that does not provide the level of specificity that other government institution have. Autonomous institutions do not have the same obligations to practice accountability and transparency as part of the state finances process, and the State Budget Law does not set out specific conditions for how they use the people's money.

In addition, the creation of autonomous institutions undermines the democratic and Constitutional mandate of National Parliament to monitor execution of public funds allocated to these autonomous institutions. One example can be seen in the 2018 General State Budget, in which the $50 million allocated to TL Cement is considered to have been executed, even though the project itself has stalled and the funds remain in the accounts of the National Mining and Petroleum Authority (ANPM).

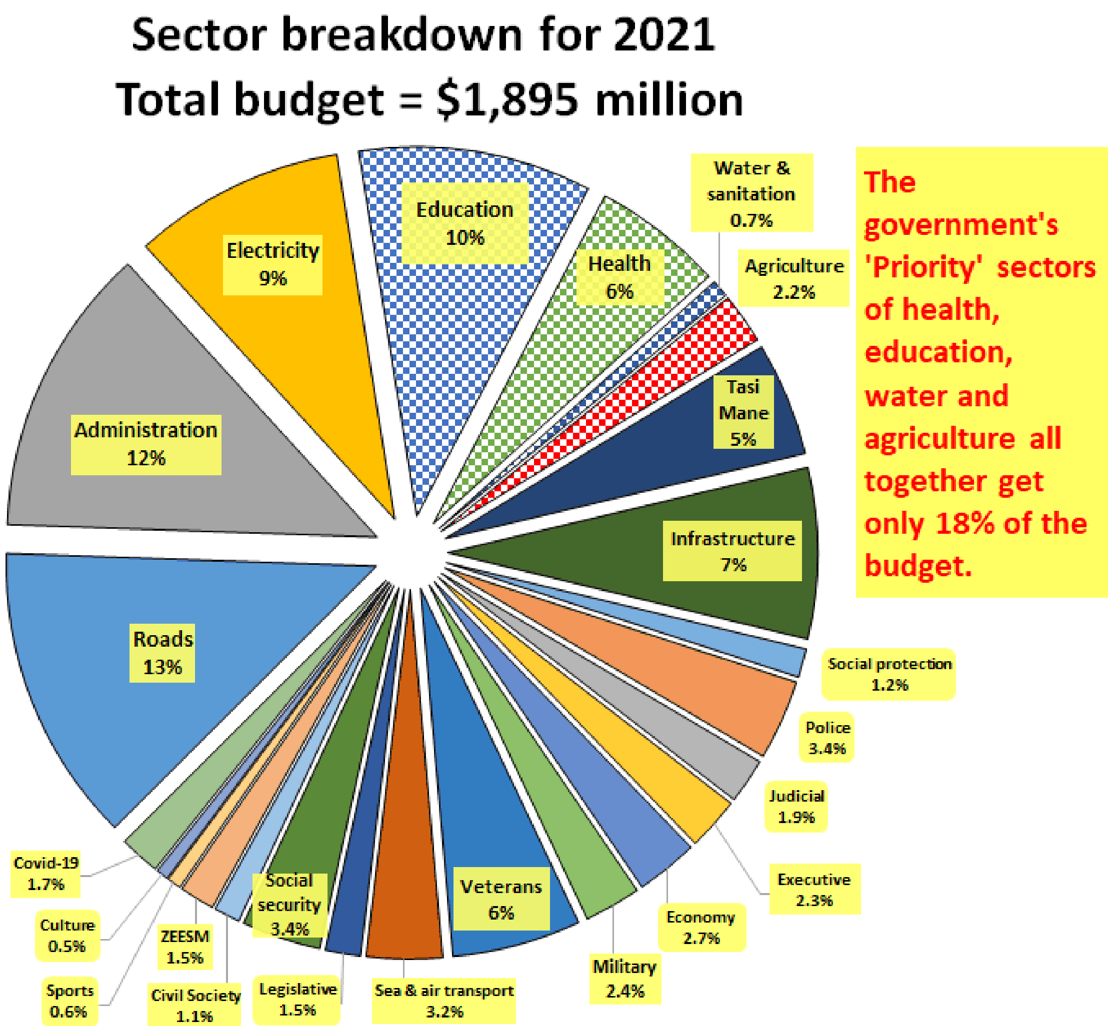
La'o Hamutuk also notes that in the proposed 2021 General State Budget, the Government proposed to spend almost 37% of the total budget through public transfers, compared with around 25% on 2018 and 2019. Government has stated its commitment to transparency and open monitoring systems, through the establishment of the Transparency Portal, Municipal Portal, and other mechanisms, but this progress will be undermined if the Government continues to reduce budget transparency and accountability and fail to implement good governance measures.

We also note that these types of allocations restrict the ability of State institutions including Government, the courts, and Parliament to oversee and monitor spending. The Transparency Portal and quarterly and annual reports on budget execution, for example, will only show a single line item. This is equivalent to a blank cheque for those in charge, and opens a path to corruption while closing the door to transparency.

We ask that the Government stop the growing trend towards public transfers, which are not transparent, and strengthen their commitment to a budgetary process that is open to popular monitoring and participation.

Invest in People to Strengthen Timor-Leste's Development

For years the Government has promised to give full attention to education, health, and clean water and sanitation. Unfortunately, this has not been reflected in General State Budgets.



Graph by La'o Hamutuk based on Ministry of Finance proposed 2021 Budget Law and Books. October 2020

We appreciate that the proposed 2021 budget slightly increases the fraction of the budget spent on these key sectors, but is still not enough to respond to the situation our people face. These allocations aim to meet the objectives of the Economic Recovery Plan. The education budget, for example, increases 69% compared with 2020, and 29% compared with 2019.

Looking at the allocation to the education sector as a proportion of overall spending, we note that the fraction of the proposed 2021 budget is 9.8%, compared with 7.3% in 2020 and 9.7% in 2019. We note that this change still fails to meet international standards which recommend that Governments spend 30% of their state budget on education and health.

Based on information in Book 2, $5.1 million of the allocation to education is for the Café Schools system, which in practice fail to give all children access to quality education. For this reason, there needs to be an evaluation prior to expanding these schools, to avoid the possibility of spending a lot of money for sub-optimal results for teachers and students.

We also note changes in allocation to other important sectors, including health which will receive $106 million, an increase of 44% compared with 2020 and 34% compared to 2019. Considering health as a proportion of the total budget, the health budget in the proposed 2021 General State Budget is 5.6% of the total, compared with 4.5% in 2020 and 5.1% in 2019. We continue to encourage the Government to invest enough to provide adequate and accessible health facilities for all of our people.

As a result of the new Program-Based Budget Model, it is difficult to ascertain total allocations to water and sanitation, as discussed above. Based on available information, the water and sanitation sector will receive only 0.7% of the total 2021 Budget. We need know how much is allocated to this important sector to better understand the Government's priorities.

We hope that the people, who deserve the State's assistance, do not have their needs prolonged by future uncertainty, as the time has come to truly invest as we discussed above, to fulfil the rights and interests of vulnerable citizens who deserve support.

Conclusion and Recommendations

We recognize that the proposed 2021 General State Budget prioritizes economic development, but that doesn't mean we should sacrifice fiscal sustainability and good governance to pursue uncertain, fantastic dreams. Based on our observations, large parts of the Government's transfers from the Petroleum Fund every year go to the State machinery. Furthermore, the Government continues to promote major projects such as the Tasi Mane project and other petroleum projects which have not yet been shown to benefit our people, nor have the future costs and risks been analysed and explained.

Therefore, we encourage the Government to consider alternative sources of revenue, by investing in productive sectors that relate to the people's real-life conditions to guarantee the sustainability of their well-being, and to relieve Timor-Leste of its dependency on oil and gas resources which will be exhausted in the near future.

We observe that although UPMA's new Program-Based Budget Model purports to be based on individual programs, it often relies of general categories. Although they include all sorts of specific activities, the new format means it's difficult for Parliament or civil society to receive detailed information. For this reason, we suggest the Parliament that this new model needs to provide specific information of each program, in order to facilitate sound decision-making and dialogue during the monitoring process, by both Parliament and the public. They would thus be able to understand what the people's money is being spent on, and what has been achieved.

We continue to be concerned with the Government's goal to create more autonomous institutions. This is not a solution for the limited achievements of Ministries, because it erodes the mandates of Government, Parliament, the courts, and the public in the process of monitoring and overseeing how the people's money is used. It would be better to resolve the internal problems in the Ministries, rather than creating new institutions that reduce transparency and violate good governance practice.

In the 2021 Budget, the Government proposes to introduce a new loan ceiling of $420 million. We suggest that Deputies exercise their mandate prior to agreeing to a loans ceiling, to understand the long-term costs after grace periods end, so that we don't create burdens for current and future generations.

We appreciate the elements that have been adopted from the Economic Recovery Plan, but we have several suggestions to adjust these measures to reflect the real and urgent conditions of the people, rather the fantasies that have long been promoted by the Government. We urge the Government to focus on important sectors including education, health, water and sanitation and those sectors that empower domestic economies including agriculture, tourism, processing industries and manufacturing.

La'o Hamutuk is always ready to offer our analytic contributions to support Deputies to have more detailed discussions about the proposed 2021 State Budget during the plenary debates, prior to its passage in the National Parliament.

Thank you for your attention and consideration.

Sincerely,

Celestino Gusmão	Eliziaria Febe Gomes	Bree Ahrens
Charles Scheiner	Marta da Silva	Adilsonio da Costa Jr.