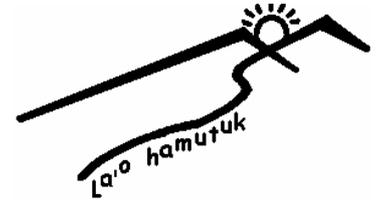


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**Submission to the  
Ministry of Natural Resources, Minerals and Energy Policy  
Democratic Republic of Timor-Leste**

**from  
La'ó Hamutuk**

**regarding the  
Policy and Guidelines for Administration and  
Monitoring of Timor-Leste Content**

**26 June 2007**

## Summary

- Money from petroleum development often does not meet people's expectations, which is one component of the "resource curse." Local content requirements, carefully planned over decades, can reduce this problem by helping to diversify Timor-Leste's economy away from dependency on petroleum revenues.
- The money for Local Content projects comes out of Timor-Leste government revenues, and should not be used to pay for oil company public relations. Company-directed projects in areas unrelated to petroleum exploration and production should not substitute for government programs.
- Local Content must prioritize items manufactured in Timor-Leste, not imported from other countries. To qualify, items should be at least 50% produced here, and at least 50% of project salaries should go to Timor-Leste citizens.
- The Timor-Leste Local Content Committee is important, but its members' terms of office, appointment process and enforcement powers should be clarified. In addition, measures must be taken to improve transparency and avoid conflicts of interest.
- Proposals to the TLCC should be published before the TLCC decides on them. Project status reports, TLCC recommendations, monitoring results, company proposals which accompany bids for contracts, and other documents should be made public not only on the internet, but also in a public information center.
- Local Content projects and procurement should be done through an open, competitive tender process.
- Vulnerable groups, especially women and children, must be protected and prioritized in Local Content projects.
- Although the mechanism used for this public consultation is better than other recent ones, it still needs improvement, especially in reaching a wider audience.

## Introduction

Once again, La'o Hamutuk would like to express our thanks to the Government and the Ministry of Natural Resources, Minerals and Energy Policy for the opportunity to participate in this public consultation. Consultations like this one exemplify the democratic and participatory foundations of our nation.

As always, La'o Hamutuk sees this consultation as an opportunity for the Government to hear diverse ideas and perspectives about the development of our country. It is very important to listen to these opinions, which can help develop good policies to minimize the risk of the "resource curse" that many countries have experienced.

La'o Hamutuk is also gratified that the Government and the Ministry understand that civil society has an important role to play in developing Timor-Leste's natural resources. We hope that this will continue, with improved mechanisms for public participation.

Regarding the proposed Policy and Guidelines for Administration and Monitoring of Timor-Leste Content, we encourage the Government to continue to develop a legal structure to implement the contracts between Timor-Leste and oil companies, to maximize the beneficial effects on the economic and social development of Timor-Leste while maintaining fiscal and ecological sustainability.

We therefore offer some ideas and recommendations about this draft decree, and we hope that the Government will consider them.

### **Often, petroleum development does not help local economies.**

Investments in the petroleum sector are very large, generating high expectations among local people, but they bring many risks. Much of the money doesn't come into the country, but goes abroad because the capacity of our economy to absorb this money is limited.

Timor Leste has already experienced this. Over the past eight years, the international community has spent close to three billion U.S. dollars on Timor-Leste, with negligible impact on the local economy. Today, Timor-Leste still imports many things from outside, because Timor-Leste does not yet produce them.

Timor-Leste does not yet have the businesses, the manufacturers, the infrastructure or the experienced workforce to supply most needs of foreign oil companies operating in our country. Even with the best of intentions, purchasers often have to rely on imports because no local sources are available.

We hope this is a temporary condition, and we encourage a long-term strategy regarding local content. Petroleum development in Timor-Leste will continue for several generations, and our human, agricultural, infrastructure and manufacturing capabilities will grow over time, increasing the absorptive capacity of our economy. We recommend that the approach and guidelines for local content include a decades-long vision, which can be achieved in stages. They should be revised periodically as our experience and absorptive capacity increases.

### **Local Content is one way to diversify Timor-Leste's economy.**

In many countries, oil projects do not benefit the local economy, but actually increase poverty. The oil companies exploit the people's resources for their shareholders' profit, but the people of the country receive little benefit from their own resources. Therefore, the State must create mechanisms to ensure that the people's interests are protected.

Like other petroleum-dependent nations, Timor-Leste needs to reduce our dependency and diversify our economy. So far, we see that Timor-Leste is receiving high revenues ("resource rent") from petroleum development, but the industry has provided few opportunities for employment or to develop the non-petroleum sector. This regulation gives legal power to the Government so that it can direct companies who exploit our resources to consider our local needs.

### **Local Content projects should not be paid for from public revenues, and oil company public relations should not substitute for government programs.**

La'o Hamutuk supports the concept of Local Content as a mechanism to strengthen and diversify Timor-Leste's economy, but we have some concerns about how to make it as effective, transparent and fair as possible.

It is important to understand that expenditures related to implementing Local Content policies are paid for by Timor-Leste. Any money spent on Local Content by a company with a Production-Sharing Contract (PSC) will be recoverable under the PSC, which means that it will be subtracted from the revenue that the State of Timor-Leste receives. As a result, Local Content projects and procurement are not paid for by the companies, but by Timor-

Leste's people. This is a fundamental fact which should be discussed in the preamble to the regulation.

In a sense, the Local Content process is a surrender of authority about how to use public money from Government to private oil companies. Although the Local Content Policy can encourage the companies to undertake projects to benefit Timor-Leste's people, it is no substitute for publicly-managed and publicly-funded programs to diversify our economy and provide public services and infrastructure. We doubt that foreign oil companies are the most qualified or motivated institutions to achieve these goals, and we strongly encourage the Timor-Leste Government to engage in a multi-sectoral, cross-ministry process to determine how public funds (both through cost-recoverable Local Content projects and Government-managed projects paid with petroleum tax revenues) can reduce petroleum dependency.

Of course, it is better for the companies to spend money in Timor-Leste rather than overseas, and for them to hire Timorese workers in preference to foreign workers. But we are concerned that such money not be wasted, or be spent only to help promote the company's popular image, since in the end it comes out of Timor-Leste's treasury, even though it bypasses the Petroleum Fund and budgeting processes.

Recently, an international oil company gave a briefing to local NGOs in Dili about "Local Content and Sustainable Development." The company discussed their "engagements" in other countries: agriculture in Nigeria, malaria control in Azerbaijan, AIDS awareness in Africa, education in Venezuela, a medical center in Libya, rice cultivation in Congo, etc. None of these have anything to do with petroleum development – but they have everything to do with reducing criticism and enhancing the company's image among the people whose resources they are profiting from.

Some of the NGOs became eager when the company mentioned that it planned to distribute \$9.5 million for "local content." Very little will be spent on purchasing goods and services, which means that most of it will be given to organizations for virtually any project they propose. The company did not mention that this would come out of Timor-Leste's revenues, as a recoverable cost, until they were directly asked.

La'o Hamutuk does not believe that petroleum company public relations, also known as co-optation, should be cost recoverable. We are glad that Articles 5(e) and 6(a) of the draft Local Content Policy include the relevance to the petroleum sector of Timor-Leste as a requirement and selection criterion for local content project proposals, but we feel that this needs to be clarified and strengthened. Expenditures which would not be made if the company had to pay for it out of their profits, or whose primary purpose is public relations, should not be recoverable or considered Local Content. Rather, Local Content should apply to decisions which the company makes in the course of its exploration and production: what goods to buy, which employees to hire, what subcontractor to use, etc. In these decisions, Timor-Leste goods, services and employees should receive priority.

Over the last eight years, Timor-Leste has experienced many poorly-coordinated projects run by the World Bank, ADB, bilateral and multilateral development partners, international NGOs and UN agencies. Gradually, our democratic government has gained some control over these projects and has begun to integrate them into the government's programs, but it has been difficult and slow.

The use of recoverable funds for company-chosen "local content" projects is a step backwards. Although the agencies listed above sometimes have secondary agendas, they

are development professionals, with a declared mission to reduce poverty or provide services. Their primary goal is to help the people the project is designed to serve.

Projects selected or run by oil companies, on the other hand, have a different objective. It doesn't matter if the project works, as long as the company defuses potential opposition and creates allies. The oil company is not staffed by development professionals; its only purpose is to make profits for its shareholders. If the company were to spend its shareholders' money on public relations projects we would gratefully accept them. But when they use money from Timor-Leste's own revenues, without making this clear, we feel manipulated. We question whether our Government should be paying foreign oil companies to select and manage projects that could be handled better by the Government using normal budgetary and administrative processes.

### **"Timor-Leste content" should really come from Timor-Leste.**

In the experience of other nations, the oil industry has little impact on the local economy, because much of the money goes to international salaries, and these highly-paid staff and consultants don't buy local products. Even the hotels they use are owned by foreigners. The salaries they receive flow right out of our country.

Because of this, we recommend that this regulation consider this risk, and include it in the policy statement. Local Content can stimulate local economic, social and infrastructure development. It is important to ensure that these investments provide socially and politically sustainable benefits to Timor-Leste.

In addition to stimulating future development and growth, local content can also be an immediate mechanism to inject money into Timor-Leste's economy and to create jobs, helping to reduce our crisis-level rates of unemployment.

We are concerned that the "acquisition of goods and services from Persons based in Timor-Leste" (Petroleum Act Article 13.3(a)(iv)) could be interpreted to include a Timor-Leste-based salesman for an international company, with negligible Timorese economic benefit. Each purchasing decision must consider this. For example, a chair could be bought from a Timorese carpentry workshop or from an importer of furniture mass-produced in Indonesia. The former helps develop our economy and provide jobs; the latter does not.

We therefore recommend that the regulation include a definition of "local goods and services" which would require that a "Timor-Leste content" purchase be at least 50% produced in Timor-Leste, and that at least 50% of the dollars paid for work and services relating to a Local Content project be paid to Timor-Leste citizens.

### **The Local Content Committee is important and must be effective.**

We support the idea of the Timor-Leste Content Committee (TLCC) to oversee the execution of the Local Content regulation.

The regulation should be clarified as to who appoints the members of the TLCC and should define their terms of office. We also recommend more clarity about the two TLCC members who can be "permanent staff" of the Government; are these chosen by the Minister to fill any of the positions listed in article 3(a) through 3(e)?

In addition, there should be provisions to reduce the risk of conflict of interest and corruption. In particular, members of the TLCC should be barred from considering proposals where they or members of their family have a potential financial interest, either as beneficiaries or competitors.

Although the TLCC can make recommendations and issue oversight reports, it has no specified enforcement powers. We recommend that the regulation specifically empower the TLCC to refer cases to the Ministry, courts, Provedor and/or Inspector General if companies provide fraudulent information to the TLCC or if they deliberately or negligently fail to follow-through on their commitments. In the absence of other legislation, the regulation should also specify penalties for such offenses which are high enough to deter multi-billion-dollar oil companies.

### **Transparency and accountability are essential.**

Transparency and accountability are very important to consider in petroleum development. The Government has shown its commitment in this area, such as requiring that all production-sharing contracts be public. However, Local Content introduces new avenues for corruption and cronyism, and we believe safeguards are necessary to prevent abuse.

We are glad that the regulation requires that the internal regulations of the TLCC, as well as proposals, evaluations and approvals be published. We suggest that proposals received by the TLCC be released at least two weeks before the TLCC makes a recommendation on them, and that the public be encouraged to submit comments before TLCC consideration and ministerial approval.

We also recommend publication of the results of TLCC monitoring (Article 10) and recommendations the TLCC makes to the Ministry, as well as the quarterly project status reports made to the TLCC.

Access to the internet is difficult for nearly all Timorese people, and the media suggested in article 9 are inadequate. We suggest that DNPG establish a publicly accessible information center, where such proposals could be read and comments accepted. Such an information center could also facilitate public awareness on other aspects of petroleum development, public tenders, as well as increasing people's understanding of these critical issues to our national economy. A public registry, as La'o Hamutuk suggested in our 2004 submission on the Petroleum Act, should also be implemented and include TLCC reports as well as PSCs and other information.

The Local Content regulation derives from Article 13 of the 2005 Petroleum Act. This Act requires that applications for production-sharing contracts include proposals for health and safety, environmental protection, training and preferential employment of Timor-Leste nationals, and acquisition of goods and services from Timor-Leste.

As we wrote in our submission on the draft Petroleum Act, companies' proposals in these areas should be published before the contract is awarded. Unfortunately, this was not incorporated into the regulation. Although Production-Sharing Contracts are published after they are awarded, these accompanying proposals have not been. We encourage the Government to publish all proposals enumerated in Article 13.3(a) of the Petroleum Act. Article 13.3(b) states that a winning applicant is "obliged to comply with its proposals," so these proposals must be considered by the TLCC when it evaluates project proposals and evaluations (Article 5 and 6 of draft Local Content regulation).

The draft Local Content regulation contains no requirement for a tender process or open competitive bidding for project proposals or to supply goods and services to those whose projects are selected. Article 12.3 of the Model Production Sharing Contract requires notice and a competitive bidding process; these should be referenced or restated in the Local Content regulation. Article 12.5 of the Model PSC requires contractors to submit information, including details of good and services procured within and outside Timor-

Leste, to the Ministry. These reports should also be provided to the TLCC and the public, and should be used by the TLCC as part of their evaluation and monitoring functions. In addition, a contractor's previous local content performance and follow-through should be a factor in evaluating their new project proposals.

### **Women and Children should not be ignored.**

We believe that the Local Content regulation needs to give attention to vulnerable groups, such as women and children. The majority of Timor-Leste's people are women, and children are the future of our nation. In this patriarchal society trying to move toward gender equality, it is important to give strong attention to women in every aspect of our nation's life.

In other countries' experience, when large investments come into the country, they don't benefit women, children and other vulnerable groups. Many times such investments reinforce the dominant position of men in the society. Many women work in their homes, and many children may leave school to seek work. Some companies exploit children, making them do heavy work. With many highly-paid foreign male workers, women may be coerced into prostitution.

We therefore recommend that the regulation include gender equity and impact in the project requirements and selection criteria.

### **The Public Consultation mechanism still needs improvement.**

Public consultation is a mechanism to facilitate public participation. We appreciate this opportunity, where the Government encourages civil society involvement, especially in the petroleum sector.

However, we continue to ask the Government to improve the public consultation process. Specifically regarding the Local Content Guidelines, we don't feel that the process facilitates broad participation or enables many people to share their ideas. Although the available languages have improved over past consultations, the Government publicized this consultation only through email and internet, which most people find difficult to access.

Therefore, we recommend that future consultations use additional media, as well as holding public hearings at national, district and subdistrict levels. The people who will produce the goods and services, or will seek training or employment in the industry, as well as those who live in communities where petroleum development may come, should be aware of this process and have an opportunity to participate.

### **Conclusion**

Finally, we would like to emphasize our perspective that this Local Content regulation is a legal mechanism to ensure that international oil companies who profit from Timor-Leste's resources also support our economy. As an oil-dependent nation, this regulation is important to help us diversify our economy by nourishing our non-oil sector. In coordination with other Government and private-sector activities, it may help Timor-Leste to avoid the worst consequences of the resource curse.