



**Democratic Republic of Timor-Leste  
IV Constitutional Government**

**EXPLANATORY STATEMENT**

**Proposed Law on First Amendments to the Law No 15/2009 of 23 December,  
approving the State Budget for the Democratic Republic of Timor-Leste for 2010.**

**Introduction**

The Government submits for consideration and approval of the National Parliament, the draft law on the First Amendment to the Law No 15/2009 of 23 December, approving the State Budget of the Democratic Republic of Timor-Leste 2010 designated Amending the State Budget for 2010.

This draft law is presented in accordance with Article 97.1 paragraph c) and Article 145.1 of the Constitution and under Article 34 and 35 of Law No 13/2009 on Budget and Financial Management. Article 34.1 of the said Act states that "The Government can propose amendments to the state budget in place when the circumstances so warrant."

Under the Act, the proposed amending budget for 2010 provides an economic perspective as well as the latest estimates of revenue and domestic oil and the estimated expenditure necessary for the Government to achieve its program and goals.

This Explanatory Memorandum is intended to provide the necessary information about the amending budget proposal and to support the deliberations of the National Parliament as well as provide details and explanations for the variations of the proposed expenditure (Annex A) and its financial table (Annex B).

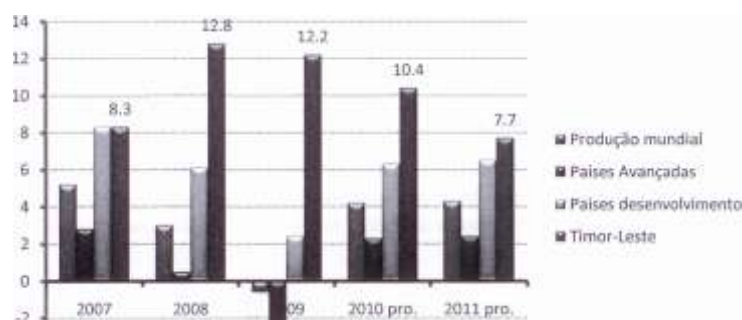
As part of the process, the government also sends to the National Parliament the reasons for the transfer of the Petroleum Fund and the report of Estimated Sustainable Income, pursuant to the Petroleum Fund Law. Certification of Estimated Sustainable Income for the External Auditor will also be sent separately, under the law.

**Economy**

**International Economy**

Despite having suffered a negative growth in 2009, the world economy, according to the *IMF's World Economic Outlook* April 2009, will grow at 4.2% in 2010. The more advanced economies are prepared for an increase of 2.3% and emerging economies and developing countries 6.3% (Chart 1). From a regional perspective, the economies of countries neighboring Timor-Leste will recover, with China to regain two digit growth, while the five ASEAN (Indonesia, Malaysia, Philippines, Thailand and Vietnam) will grow cumulatively about 4.7%. With regard to major regional economies, Singapore is expected to grow at 5.7% and Australia 3%.

**Chart 1: Overview of Global Economic Growth: 2007-2011**



Sources: IMF, World Economic Outlook, April 24, 2010; National Directorate of Macro Economics - Department of Finance.

Year	2007	2008	2009	2010 pro.	2011 pro.
World production	5.2	3	-0.6	4.2	4.3
Advanced Countries	2.8	0.5	-3.2	2.3	2.4
Developing countries	8.3	6.1	2.4	6.3	6.5
Timor-Leste	8.4	12.8	12.2	10.4	7.7

After low inflation rates in 2009, there will be relatively moderate price increases during 2010. With respect to major trading partners of Timor-Leste, Indonesia is expecting a Consumer Price Index rise of 4.7%, Singapore 2.1% and Australia 2.4%.

## National economy

### Non-Oil GDP

The economy of Timor-Leste has expanded rapidly in recent years, caused by a rapid increase in public investment in the areas of electricity, health, education, housing and human capital as well as an expansion of the private sector since 2007. After growth of 8.4% since 2007, real non-oil GDP (excluding the UN) grew 12.8% in 2008 and approximately 12.2% in 2009 according to preliminary estimates by the Government. The supply of high-yield seeds, fertilizers and tractors contributed to increased production and productivity of the agricultural sector in 2009. The Private Sector also began contributing to GDP growth, especially telecommunications and transport, and it is expected that the pace of growth remains in double digits in 2010.

### Inflation

The annual estimate of March 2010 the Consumer Price Index was 3.7%. Primarily responsible for this number was increasing prices in the housing sector (9.9%), cereals, tubers and their derivatives (7.0%) and transport (5.7%). Inflation in some sectors not covered by the Consumer Price Index, especially construction materials, it is expected to be higher due to high demand in 2009.

### Aggregate Government Expenditure

Execution of the 2009 Budget totaled \$604.4 million (in cash). The amount of expenditure in 2009 represented an increase of 9.3% compared to 2008, including a 5% increase in current expenditure and 17.9% in expenditures for capital development.

For the year 2010, the proposed amendment of the Budget will increase the level of expenditure to \$837,981 million.

**Table 1. Expenditure for the entire Government, 2008 - 2010 (\$millions)**

<b>Expenditure</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2010 rectification</b>
<b>Total Expenditure</b>	<b>788.3</b>	<b>680.9</b>	<b>660.0</b>	<b>838.0</b>
Recurrent Expenditure	638.5	437.4	413.4	552.5
Salaries and Wages	58.9	93.8	97.7	99.1
Goods and Services	447.4	247.3	210.3	268.8
Transfers	132.2	96.4	105.4	184.6
<b>Capital Expenditure</b>	<b>149.8</b>	<b>243.4</b>	<b>246.6</b>	<b>285.5</b>
Minor Capital	39.2	38.1	29.8	34.5
Capital Development	110.6	205.4	216.8	251.0

Sources: Timor-Leste - Ministry of Finance, Department of Macroeconomics

### **Domestic revenue**

It is expected that domestic revenues will grow from \$87 million dollars in 2009 to \$94.8 million in 2010. It is further expected that domestic revenues continue to grow while also improving the mechanisms for revenue collection. For Autonomous Bodies, fees and taxes also showed an increase due to solid growth and better performance in revenue collection in 2010. Domestic revenues in 2010 varied according to Table 2, below.

**Table 2: Domestic Revenues, 2009-2013  
(\$Million)**

	2009	2010	2011	2012	2013
	Actual	Projections based on 2010 budget and actual numbers of 2009			
<b>Domestic Revenue</b>	<b>27.3</b>	<b>28.0</b>	<b>33.0</b>	<b>38.0</b>	<b>43.0</b>
Customs revenue	16.3	19.5	22.7	25.9	29.1
Domestic Tax	11.9	14.1	16.3	18.4	20.6
User Fees and Other Revenue	20.7	20.1	12.8	5.5	0.4
Dividends and Interest	10.7	13.0	16.0	18.8	21.7
Autonomous Bodies	27.3	28.0	33.0	38.0	43.0

Sources: Timor-Leste, Ministry of Finance, Treasury Department and the Budget 2009 for real values; Directorate macroeconomic projections for 2010.

Despite the increase in rice production in 2009, the deficit of rice continued. Thus, the Government will continue to subsidize sales of rice in 2010, however, a substantial reduction of these subsidies is expected in 2011.

### **Fees and Taxes**

Total revenues from fees and taxes increased 93% in 2009, despite the moderation of this growth, it will remain at approximately 18.5%. This is a result of continued economic expansion and improving the Government's fiscal performance.

**Table 3: Income from fees and taxes**

	2008	2009	2010	2011	2012	2013
	Actual		Projections based on 2010 budget and actual numbers of 2009			
<b>Fees, taxes and other revenue</b>	<b>6.2</b>	<b>11.9</b>	<b>14.1</b>	<b>16.3</b>	<b>18.4</b>	<b>20.6</b>
Company Registration	0.3	0.2	0.5	0.5	0.6	0.7
Post office	0.0	0.0	0.0	0.0	0.0	0.1
Fees for Land and Property	1.5	1.9	2.8	3.3	3.7	4.1
Fees for Water and Sanitation	0.0	0.1	0.1	0.1	0.1	0.1
Tuition at the National Univ.	0.4	0.4	0.7	0.8	0.9	1.0
Vehicle Inspection Fees	0.3	1.0	0.9	1.0	1.2	1.3
Vehicle Inspection Fees	0.1	0.0	0.2	0.2	0.2	0.2
Driving License Fees	0.2	-	0.3	0.3	0.3	0.4
Other Transport Fees	0.0	0.0	0.0	0.0	0.0	0.0
Passports and Identity	0.3	0.4	0.6	0.7	0.8	0.9
Visas	1.0	1.2	1.8	2.1	2.4	2.7
Hospital Revenue	0.1	0.1	0.1	0.1	0.1	0.1
Dividends, Profits and Earnings	1.8	4.6	4.8	5.5	6.2	7.0
Taxes on Mineral Extraction	0.0	0.1	0.0	0.1	0.1	0.1
Taxes on radio and television	-	-	-	-	-	-
Receipts for documents under concursos	0.1	0.1	0.1	0.1	0.1	0.2
Government Equipment Auction						
Other	0.1	1.9	1.2	1.4	1.6	1.8

Sources: Timor-Leste, Ministry of Finance, Treasury Department and the Budget 2009 for real values; Directorate macroeconomic projections for 2010.

Revenues from fees and taxes can have a rapid increase, based on increased rates and properly managed contracts and collection of revenues. This is an area that the Government will also seek to improve.

One challenge for reform in this area is the coordination, as there are more than seventeen types of revenue collected by different government departments. In this sense, future reforms should include the establishment of mechanisms for coordination and control to share information and improve the planning process in this area.

### **Autonomous Bodies**

It is expected that revenue growth of autonomous bodies remain strong in 2010 at a rate of 21.5%. It is expected that these increases will continue over the medium to long term while EDTL continues to expand global economic growth increases the income of all the autonomous bodies. The Institute of Equipment Management will adopt a model of providing its free services, since this seems to be more efficient model.

Nevertheless, there is strong potential for increased revenue for EDTL, while good management continues to increase control and ensure that all homes and businesses are within the system. EDTL is one of the organizations that receives more subsidies from the state budget since it has a deficit of

about \$30 million a year. The Government intends to reduce these values in the coming years, increasing its own revenues and thus reducing dependence on transfers from the Petroleum Fund.

**Table 4: Revenues of Autonomous Bodies**

	2008	2009	2010	2011	2012	2013
	Actual		Projections based on the 2010 budget and current figures for 2009			
<b>Revenues of Autonomous Bodies</b>	<b>7.6</b>	<b>10.7</b>	<b>13.0</b>	<b>15.9</b>	<b>18.8</b>	<b>21.7</b>
Administration of Airports and Air Navigation TL	0.7	1.0	1.2	1.4	1.7	1.9
Port Authority of Timor-Leste	1.8	1.6	2.5	3.0	3.6	4.1
Electricity of Timor-Leste	5.1	8.2	9.4	11.5	13.6	15.7
Institute of Equipment Management (IGE)						

Source: Timor-Leste, Ministry of Finance, Treasury Department and the Budget 2009 for real values; Directorate macroeconomic projections for 2010.

### Oil Revenues

Oil revenues for the year 2009 totaled \$1,660 million, of which \$994 million was from royalties and benefits from oil and gas, \$661 million in fees for oil and \$5 million others. The final balance in the Petroleum Fund on December 31, 2009 was \$5,377 million, \$107 million higher than the estimate provided in Budget 2010.

The average real price of oil in 2009 was \$62 per barrel, which means it was \$2 per barrel higher than projected in the budget. The average price of WTI crude oil for the first four months of 2010 was \$80 dollars, but recently dropped significantly. In late May 2010, the WTI oil price is \$74 per barrel but it has lately been very volatile. Oil revenues in the first four months were \$651 million, the net return on investment of \$67 million and raising \$150 million. The closing balance at the end of April 2010 was \$5.945 million.

In Table 4 below, the oil revenues for 2009 are depicted along with updated estimates of oil revenues and net investment return for 2010, and the estimated final balance of the Petroleum Fund for 2010. The estimates are based on actual data for the first four months of 2010 and the amount of withdrawals proposed by the Government for 2010.

Due to the higher than expected oil price, the estimated average price per barrel for 2010 increased from \$62 to \$68, which resulted in an increase of \$450 million of the estimated revenues from petroleum. The planned production and net return on investment for 2010 remain.

**Table 5: Petroleum Fund in 2009 and 2010**

\$Million	2009		2010	
	Budget 2009	The current numbers	Budget 2010	Amending
<b>Opening Balance</b>	<b>4,197</b>	<b>4,197</b>	<b>5,270</b>	<b>5,377</b>
Petroleum receipts	1,460	1,660	1,244	1,694
Net Return	21	32	147	147
Withdrawals	408	512	502	811
<b>Ending Balance</b>	<b>5,270</b>	<b>5,377</b>	<b>6,159</b>	<b>6,407</b>

The updated estimate gives an ending balance of the Petroleum Fund of \$6,407 million at the end of 2010.

The Government did not update its revenue projections for the Fund after 2010, before submitting the amended budget to Parliament. The next revision of the Petroleum Wealth and Income Estimate will be made before the presentation of the 2011 Budget by the Government.

### **Details of expenditure and new measures**

The Government proposes additional measures and essential to achieve its objectives in 2010. These include taking advantage of new opportunities to achieve Government priorities, particularly to expedite national economic development which is the most effective way to increase the general welfare.

The Rectification Budget also includes some urgent and unavoidable expenses which could not be foreseen when the State Budget was presented to the National Parliament on 15 October 2009.

Most of the additional expenses are for infrastructure, tourism, commerce and industry, social welfare, state administration and whole of government.

The total increase in expenditure in the rectified budget is \$177,985,000. This increase is concentrated in the categories of Capital Development (\$34,201,000), goods and services (\$58,470,000) and Public Transfers (\$79,241,000 which includes \$31,356,000 transferred from Ministerial lines to the Package for Decentralized Development).

The Package for Decentralized Development was approved by Decree-Law No. 2/2010 of 18 February, which approves special procedures for award of civil works of value up to USD \$250,000 to local companies based in the Sub-Districts .

Some major new measures, by expense category, are as follows:

#### Capital Development

This category refers to expenses necessary to make the investments to develop the basic infrastructure of Timor-Leste:

- Purchase of generators to increase the capacity of the Comoro power station and ensure a more reliable power supply to Dili (\$10,000,000)
- Continued Government commitment to developing an integrated system to ensure financial accountability and greater transparency (\$7,300,000);
- The construction of barracks for the Naval Component of Hera and the docks necessary for the new patrol boats (\$8,350,000);
- First phase of rehabilitation of the runway of the airport in Dili (\$2,000,000).

#### Goods and Services

This category aims to purchase goods and services that Timor-Leste does not produce in sufficient quantities.

- Food security through the purchase, storage and distribution of rice (\$17,500,000);
- Allowance for students in Cuba (\$1,900,000)
- Continue to support education by strengthening the Feeding Program in schools and language program (\$1,125,000);

## Public transfers

This category refers to payments related to poverty reduction and targeting those who live in financially difficult circumstances but who have an important role in building the country

- Payments to veterans (\$25,510,000), pursuant to law;
- Resolution of pending cases relating to internally displaced persons (\$4,000,000);
- Natural Disasters (\$1,000,000);
- Medical treatment abroad (\$2,000,000);
- Demolition of buildings in Timor-Leste (\$5,500,000);
- Payment for the new diocese of Maliana and renovation of churches in the districts (\$3,500,000).

Relatively small amounts are expected for the category of Minor Capital for equipment purchases and transportation, and for payment of salaries to civil servants.

These initiatives are in accord with the objectives of the Government for 2010 and the priority areas set out in the Summary of the Strategic Development Plan of the Government. In particular the Government is committed to achieving the strategic investments in infrastructure projects which contribute to the objective of national development.

Food security of the people of Timor-Leste is a priority for the Government. In the short term we need to seek foreign markets to ensure the supply of the Country. It is expected that Timor-Leste will levels reach self-sufficiency through increased productivity: agricultural diversification and strengthening of trade.

The Rectified Budget also includes the reallocation of resources between ministries to meet the Government's program and to reach the objectives for this proposal. These reallocations do not increase costs, but they comprise measures for better financial management.

Annex A to this Explanatory Memorandum provides a complete list of all variations of proposed expenditures for the amended budget by agencies and categories and their detailed justifications.

A new list of appropriations that reflect all these variations of expenses and transfers carried out is in Annex II to the draft law amending budget for 2010.

by the Council of Ministers on May 31, 2010

/ s /

The Prime Minister  
Kay Rala Xanana Gusmão

/ s /

The Minister of Finance  
Emilia Pires