

ASIAN DEVELOPMENT BANK

TAR:TIM 38190

TECHNICAL ASSISTANCE

TO THE

DEMOCRATIC REPUBLIC OF TIMOR-LESTE

FOR

STRENGTHENING FINANCIAL MANAGEMENT CAPACITY

December 2004

CURRENCY EQUIVALENTS

Currency unit – US dollar (\$)

As of August 2001 the legal tender of Timor-Leste is the US dollar.

ABBREVIATIONS

ADB	–	Asian Development Bank
MPF	–	Ministry of Planning and Finance
NDP	–	National Development Plan
NDPEAC	–	National Directorate for Planning and External Assistance Coordination
SIP	–	sector investment programs
TA	–	technical assistance

TECHNICAL ASSISTANCE CLASSIFICATION

Targeting Classification	–	Targeted intervention
Sector	–	Law, economic management and public policy
Subsector	–	Public finance and expenditure management
Theme	–	Governance
Subtheme	–	Financial and economic governance

NOTES

- (i) The fiscal year (FY) of the Government ends on 30 June.
- (ii) In this report, "\$" refers to US dollars.

This report was prepared by H. Baxter, Pacific Department.

I. INTRODUCTION

1. The Government of Timor-Leste has made considerable progress in economic and financial management since independence in 2002. Implementation of the National Development Plan (NDP) and road map is being achieved, and the Government is enhancing decision-making through the use of comprehensive sector analyses and the formulation of sector investment programs (SIPs), which identify investment opportunities for both Government and development partners. Considerable challenges remain in this area, despite the considerable achievements to date.

2. The current assistance program of the Asian Development Bank (ADB) identifies capacity development in economic management as a priority focus area. ADB has provided assistance in this sector since 2001. Key technical assistance (TA) grants¹ have supported the Government in economic and financial management. The Government has appreciated, in particular, the expertise provided by the petroleum fiscal adviser to the Prime Minister's Department on the issue of Timor Sea revenues. The Ministry of Planning and Finance (MPF) has received valuable assistance for the development of SIPs in the energy, transport, communications, and water sectors; and in the overall management and coordination of the SIP exercise. Support to MPF to improve monitoring of NDP implementation includes the provision of better tools, and development of in-house skills and competency to assist line ministries in planning and delivery of their programs. A common recommendation emerging from these TAs is that additional support is required to entrench the capacity already developed in these key government units and to enable them to respond to the immediate and medium-term challenges facing the Government.

3. This TA² will improve the Government's capacity for economic and financial planning and management by continuing to support NDP implementation and the management of petroleum revenues.

4. During the Country Programming Mission in March 2004, the Minister for Planning and Finance endorsed the TA. The Fact-Finding Mission fielded in September 2004 finalized TA design and discussed the rationale, objectives, scope, cost estimates, and implementation arrangements with MPF. In December 2004, the Government agreed to the TA. The TA framework is attached as Appendix 1.

II. ISSUES

5. The Government is striving to build its economy and develop a responsible and responsive government with an efficient, effective and accountable civil service from the point of view of donor harmonization and alignment. Many development partners including ADB, World Bank, United Nations, and bilateral agencies of the governments of Australia, the European Union, Portugal, and United States, among others, are actively involved in supporting public sector management. Challenges exist in several areas, notably budget planning and allocation, budget execution, and expenditure control and accountability mechanisms. The withdrawal of international advisers has lent urgency to the development of a well-designed, sustainable

¹ ADB. 2000. *Technical Assistance to East Timor for Strategies for Economic and Social Development*. Manila; ADB. 2001. *Technical Assistance to East Timor for Economic Policies and Strategies for Development Planning*. Manila; ADB. 2002. *Technical Assistance to Timor-Leste for Capacity Building to Develop Public Sector Management and Governance Skills*. Manila; ADB. 2004. *Technical Assistance to Timor-Leste for Capacity Building in the Ministry of Planning and Finance to Monitor the National Development Plan*. Manila.

² The TA first appeared in the *ADB Business Opportunities* (Internet edition) on 27 October 2004.

capacity-building program in financial management across government. The Government has asked the World Bank to lead development partners with an interest in public financial management to jointly support the development of an integrated and long-term financial management capacity-building Program. ADB supports the concept of a joint integrated initiative to ensure that the efforts of development partners are coherent from the point of view of donor harmonization and alignment. This initiative is still in the planning phase and ADB is monitoring the progress.

6. A number of key issues can and should be addressed now. The Government's draft priorities and proposed SIP for public sector management identifies the critical need for strengthened planning processes and a more comprehensive budget framework for revenue capture and expenditure management.

7. **Strengthened planning and monitoring.** The National Directorate for Planning and External Assistance Coordination (NDPEAC) in MPF is the lead unit responsible for overall supervision of the Government's planning process, including oversight of the agency-level annual action plans, the SIP exercise, and preparation of the next 5-year national development plan. It is continuing to develop and implement a comprehensive, government-wide information system to monitor NDP progress, and to provide a central repository of information on donor-funded projects. Complementing its planning mandate, NDPEAC is also responsible for overall coordination of external assistance to Timor-Leste. NDPEAC has a demanding work program over the next 4 years, and the Government has requested ongoing support for its work.

8. In the immediate short term, the Government needs to finalize the SIP process before the next Timor-Leste and development partners meeting. For the process to be of value in the long term, however, the Government needs to mainstream this process as an integral part of the annual budget process. For this to happen, NDPEAC must be able to take the lead in supporting all government agencies in their planning and monitoring of the programs for which they are responsible through the annual action plan processes. NDPEAC also must be able to optimize the utility of the systems and documentation for planning and monitoring.

9. **Fiscal management.** Petroleum revenues will be important to Timor-Leste's economic development. International experience, however, indicates that natural resource riches can be a cause for concern. Timor-Leste has adopted prudent policies regarding the management of petroleum and has committed to transparent and accountable operations for the management and tax regime for the extraction of oil and gas, and the management of the financial savings via a petroleum fund. The United States Agency for International Development and ADB have given the Government considerable support. The Government has drafted a fiscal policy framework and a savings policy, and is considering a proposal for a petroleum fund. An extensive public consultation process is under way. The Council of Ministers will propose the draft legislation for the petroleum fund to the Parliament in early 2005.

10. Future developments in this area will need to include an assessment of the results of the consultation process and the incorporation of that feedback into the Government's next steps. The implementation of the legislative and policy framework is critical. Sound revenue forecasting is vital to the Government's economic management and budget planning process and is of great interest to the development partner community. The Government will face several critical decisions in this area and will be relying on the best possible information to make sound decisions. The Government has indicated that continuing support is vital.

III. THE TECHNICAL ASSISTANCE

A. Purpose and Output

11. The goal of the TA is to achieve competent public administration and effective government. Its purpose is to improve government capacity for economic and financial planning and management.

12. Specific outputs will include (i) capacity development in implementing the NDP, including improving tools and skills for planning, monitoring and reporting programs, activities and performance at agency level; and (ii) capacity development in economic and financial management of petroleum and natural gas revenues.

B. Methodology and Key Activities

13. To develop capacity in implementing the NDP, consulting services will be provided to undertake the following activities: (i) support NDPEAC officials in implementing the SIP process to finalization for the 2005 Timor-Leste and Development Partners Meeting; (ii) prepare user guidelines and training materials for implementation of the Government's reporting and information management system (GRIMS); (iii) design, develop, and implement a train-the-trainer program for NDPEAC staff responsible for supporting line ministry focal points; and (iv) advise on preliminary preparations for next NDP.

14. To develop capacity in economic and financial management of petroleum and natural gas revenues, consulting services will be provided to undertake the following activities: (i) advise on the implementation of the proposed fiscal regime and gas valuation methodology for gas projects; (ii) advise on fiscal, economic, and financial matters affecting Timor-Leste's interests in oil and gas projects; (iii) advise on the regulatory and fiscal provisions for natural gas development in the Timor Sea; (iv) advise on possible fiscal frameworks for management of future petroleum revenues; (v) advise on revenue forecasts from the Timor Sea for budget and fiscal planning purposes, including the preparation of financial models of the main petroleum projects under consideration in the Joint Petroleum Development Area of the Timor Sea; (vi) participate in negotiations over petroleum matters with current and potential investors, or with other governments and international organizations; and (vii) promote awareness of petroleum fiscal issues among government personnel in Timor-Leste and development of skills in petroleum economic matters for Timor-Leste officials.

C. Cost and Financing

15. The total cost of the TA is estimated at \$295,000 equivalent. ADB will finance \$250,000 and the balance of \$45,000 will be provided by the Government through the provision of counterpart staff, support services, office facilities, and seed supplies. The TA will be financed on a grant basis by ADB's TA funding program. Detailed cost estimates and the financing plan are in Appendix 2.

D. Implementation Arrangements

16. MPF will be the Executing Agency. The TA will be implemented in close cooperation with the Office of the Prime Minister and the Timor Sea Office.

17. The TA will be implemented over 24 months beginning 1 February 2005, and is expected to be completed by 31 January 2007.

18. One international consultant will have expertise in public financial management and budget planning, and demonstrated capability in transferring skills and knowledge. The consultant will provide 2 person-months of input. One international consultant will have expertise in fiscal management in the petroleum and gas industry, and provide 1.5 person-months of input. Short-term consultants will be recruited based on areas identified when the capacity development program is developed, and will provide a total of 4 person-months of consulting services. Outline terms of reference are in Appendix 3. The consultants will be engaged by ADB on an individual basis in accordance with its *Guidelines on the Use of Consultants*. The consultants will provide inception, progress, and final reports to ADB.

19. The results of the assistance will be disseminated throughout the government in Timor-Leste and to key stakeholders including the country's development partners.

IV. THE PRESIDENT'S DECISION

20. The President, acting under the authority delegated by the Board, has approved the provision of technical assistance not exceeding the equivalent of \$250,000 on a grant basis to the Government of Timor-Leste for Strengthening Financial Management Capacity, and hereby reports this action to the Board.

TECHNICAL ASSISTANCE FRAMEWORK

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions
<p>Goal Competent public administration and effective government</p>	<p>Government of Timor-Leste administers government programs requiring minimal external assistance by 2010</p>	<p>Asian Development Bank (ADB) Outlook Report Timor-Leste annual government report to development partners</p>	
<p>Purpose Improve Government capacity for economic and financial planning and management</p>	<p>Ministry of Planning and Finance (MPF) manages the sector investment programs (SIP) process Petroleum Fund arrangements are implemented by end 2006</p>	<p>Timor-Leste annual government report to development partners</p>	<p>Complementary support from other international development agencies will continue.</p>
<p>Outputs</p> <p>Output A: Capacity development in implementing the National Development Plan (NDP), including improved tools and skills for planning, monitoring, and reporting programs, activities, and performance at the agency level</p> <p>Output B: Capacity building in economic and financial management of petroleum and natural gas revenues</p>	<p>SIP process is completed on-time for the NDP in 2005 Line ministries demonstrate ownership of annual action plans, and utilize plans and reports for budget planning process in 2005 Government implements the Petroleum Fund legislation by end 2005</p>	<p>Timor-Leste annual government report to development partners Development partner feedback on quality of SIP documentation Timor-Leste annual government report to development partners International Monetary Fund (IMF) reports</p>	<p>Competent and committed counterpart staff will be available. The Government will continue to keep the process transparent.</p>
<p>Activities</p> <p>Output A activities: (i) Support National Directorate for Planning and External Assistance</p>	<p>SIP process is complete by June 2005</p>	<p>Timor-Leste annual government report to development partners Feedback from</p>	

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Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions
<p>Coordination (NDPEAC) officials in implementing the SIP process to the preparation stage for the next Timor-Leste ad development partners meeting.</p>		development partners	
<p>(ii) Prepare user guidelines and training materials for implementation of the Government reporting and information management system (GRIMS).</p> <p>(iii) Design, develop and implement a train-the-trainer program for NDPEAC staff responsible for supporting line ministry focal points.</p> <p>(iv) Advise on preliminary preparations for the next NDP</p> <p>Output B Activities:</p> <p>(i) Advise on implementation of the proposed fiscal regime and gas valuation methodology for gas projects</p> <p>(ii) Advise on fiscal, economic, and financial matters affecting Timor-Leste's interests in oil and gas projects</p> <p>(iii) Advise on the regulatory and fiscal provisions for natural gas development in the Timor Sea</p> <p>(iv) Advise on possible</p>	<p>Guidelines and training programs are delivered to target users of GRIMS by end 2005</p> <p>NDPEAC staff deliver training programs to target officials.</p> <p>Line ministry staff are competent users of planning and monitoring tools</p> <p>NDPEAC has drafted strategy for the preparation of 2nd NDP by end 2006</p> <p>Advice accepted by the Government</p> <p>Advice accepted by the Government</p> <p>Advice accepted by the Government Acceptance by IMF</p> <p>Advice accepted by the</p>	<p>Training evaluations</p> <p>Training evaluations</p> <p>Feedback from ministers and secretaries of state</p> <p>Annual Action Plan of MPF</p> <p>Timor-Leste annual government report to development partners</p> <p>Timor-Leste annual government report to development partners</p> <p>Timor-Leste annual government report to development partners IMF reports</p> <p>Timor-Leste annual</p>	<p>GRIMS development finalized</p> <p>Line ministry staff are identified and released for training</p>

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Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions
fiscal frameworks for management of future petroleum revenues	Government Acceptance by IMF	government report to development partners IMF reports	
<p>(v) Advise on revenue forecasts and prepare financial models of the main petroleum projects under consideration in the Timor Sea</p> <p>(vi) Participate in negotiations over petroleum matters with current and potential investors, or with other governments and international organizations.</p> <p>(vii) Promote awareness of petroleum fiscal issues among government personnel in Timor-Leste and development of skills in petroleum economic matters.</p>	<p>Advice accepted by the Government</p> <p>Financial models prepared and accepted by IMF</p> <p>Negotiations are successfully concluded and satisfactory progress made where resolution is not achieved</p> <p>Government officials with petroleum fiscal responsibilities are aware of key issues</p>	<p>Timor-Leste annual government report to development partners</p> <p>IMF reports</p> <p>Timor-Leste annual government report to development partners</p> <p>Feedback from relevant ministers and officials</p>	
<p>Inputs ADB technical assistance grant of \$250,000, of which</p> <p>(i) Consultants \$158,000 (ii) Travel \$50,000 (iii) Reports, training, seminars, and conferences, miscellaneous administration and support costs \$19,000 (iv) Contingencies \$23,000</p>			

COST ESTIMATES AND FINANCING PLAN
(\$'000)

Item	Foreign Exchange	Local Currency	Total Cost
A. Asian Development Bank Financing^a			
1. Consultants			
a. Remuneration and Per Diem	158.0	0.0	158.0
b. International Travel	50.0	0.0	50.0
c. Reports and Communications	8.0	0.0	8.0
2. Training, Seminars, and Conferences	8.0	0.0	8.0
3. Miscellaneous Administration and Support Costs	3.0	0.0	3.0
4. Contingencies	23.0	0.0	23.0
Subtotal (A)	250.0	0.0	250.0
B. Government Financing			
1. Office Accommodation and Transport	0.0	5.0	5.0
2. Remuneration and Per Diem of Counterpart Staff	0.0	35.0	35.0
3. Others	0.0	5.0	5.0
Subtotal (B)	0.0	45.0	45.0
Total	250.0	45.0	295.0

^a Financed by the Asian Development Bank's technical assistance funding program.
Source: Asian Development Bank estimates.

OUTLINE TERMS OF REFERENCE FOR CONSULTANTS

A. Public Financial Management Specialist / Planning Specialist (international, 2 person-months)

1. The Specialist will have expertise in public financial management and budget planning.
2. The specific responsibilities of the specialist include the following:
 - (i) support the Ministry of Planning and Finance in the implementation of the National Development Plan;
 - (ii) assist the Ministry of Planning and Finance in the development of sector expenditure programs;
 - (iii) assist the Ministry of Planning and Finance in preparing for and conducting negotiations with development partners on possible investments;
 - (iv) identify knowledge and skill requirements of National Directorate for Planning and External Assistance Coordination staff and other gaps in capability and make recommendations and plans to develop appropriate capacity; and
 - (v) promote awareness of the sector expenditure program among government personnel and contribute to the development of knowledge and skills in the budget planning process.

B. Fiscal Management Specialist (international, 1.5 person-months)

3. The Specialist will have expertise in fiscal management in the petroleum and gas industry and other related areas.
4. The specific responsibilities of the specialist include the following:
 - i) advise on the implementation of the proposed fiscal regime and gas valuation methodology for gas projects;
 - ii) advise on fiscal, economic, and financial matters affecting Timor-Leste's interests in oil and gas projects;
 - iii) advise on the fiscal implications for Timor-Leste in negotiations over territorial or jurisdiction arrangements in the Timor Sea;
 - iv) advise on the regulatory and fiscal provisions for natural gas development in the Timor Sea (including gas transportation);
 - v) Advise on possible fiscal frameworks for management of future petroleum revenues;
 - vi) advise on revenue forecasts from the Timor Sea for budget and fiscal planning purposes, including the preparation of financial models of the main petroleum projects under consideration in the Joint Petroleum Development Area of the Timor Sea;
 - vii) participate, as required, in negotiations over petroleum matters with current and potential investors, or with other governments and international organizations; and

- viii) promote awareness of petroleum fiscal issues among government personnel in Timor-Leste and development of skills in petroleum economic matters for Timor-Leste officials.

C. Short-Term Consultants (international, 4 person-months)

5. Short-term consultants or facilitators will be recruited based on areas identified when the capacity development program is developed. The detailed terms of reference and qualifications will also be determined during this stage.

D. Reporting Requirements

6. The consultants will provide inception, progress, and final reports to the Asian Development Bank.