RISK ASSESSMENT AND RISK MANAGEMENT PLAN (SUMMARY)

1. This plan has been prepared to support implementation of the Second Governance and Anticorruption Action Plan of the Asian Development Bank (ADB). It provides a summary assessment of governance issues in Timor-Leste and identifies the main governance-related risks in the areas of public financial management, procurement, and corruption. The plan includes (i) actions that ADB can take to manage or mitigate each governance risk, and (ii) indicators to monitor implementation.

A. Governance

2. During 2007–2014, Timor-Leste registered significant improvements in the political stability and regulatory quality dimensions of the Worldwide Governance Indicators. Table 1 compares Timor-Leste’s scores for each indicator in 2014 with the average scores for ADB’s developing member countries in Asia and the Pacific.

<table>
<thead>
<tr>
<th>Country or region</th>
<th>Voice and Accountability</th>
<th>Political Stability</th>
<th>Government Effectiveness</th>
<th>Regulatory Quality</th>
<th>Rule of Law</th>
<th>Control of Corruption</th>
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</thead>
<tbody>
<tr>
<td>Timor-Leste</td>
<td>0.11</td>
<td>(0.22)</td>
<td>(1.16)</td>
<td>(0.89)</td>
<td>(1.17)</td>
<td>(0.84)</td>
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<tr>
<td>Average for developing member countries Pacific</td>
<td>0.69</td>
<td>0.55</td>
<td>(0.63)</td>
<td>(0.90)</td>
<td>(0.75)</td>
<td>(0.29)</td>
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<td>Developing Asia</td>
<td>(0.80)</td>
<td>(0.42)</td>
<td>(0.36)</td>
<td>(0.55)</td>
<td>(0.55)</td>
<td>(0.57)</td>
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</table>

The indicators are measured in the range of –2.5 to 2.5, with a higher score indicating better governance.

The Pacific comprises the Cook Islands, Fiji, Kiribati, the Marshall Islands, the Federated States of Micronesia, Nauru, Palau, Papua New Guinea, Samoa, the Solomon Islands, Timor-Leste, Tonga, Tuvalu, and Vanuatu.


B. Public Financial Management

3. Timor-Leste’s public financial management (PFM) systems were assessed with the Public Expenditure and Financial Accountability (PEFA) framework in 2010 and 2013. The 2013 PEFA assessment confirmed improvements in 11 of the 31 PFM indicators with notable improvements in the comprehensiveness of fiscal information, fiscal transparency, the use of an integrated financial management information system and a treasury single account. Timor-Leste has also maintained a robust and transparent framework for managing petroleum revenues.

4. The Budget and Financial Management Law 2009 and the 2015 Organic Law of the Ministry of Finance (MOF) define the core regulatory framework for PFM. The government has completed legislative reforms to strengthen budget and financial management, personnel management, and petroleum management. Key developments include restructuring of the MOF, establishment of the Public Service Commission and Anti-Corruption Commission (ACC) in 2009, and establishment of the National Procurement Commission (NPC), National...

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Development Agency, and Major Projects Secretariat in 2011. Legislative scrutiny of the external audit process has also improved.

5. The 2013 PEFA assessment and 2015 Public Expenditure Review identified the following PFM weaknesses: (i) limited budget credibility, with high deviations in aggregate expenditure and relatively high variance in expenditure composition; (ii) weak budget forecasting processes, particularly with regard to links between capital expenditure and future operating costs; (iii) limited capacity to select and execute large infrastructure projects.⁵

C. **Procurement**⁶

6. The Procurement Legal Regime consists of Decree Law no. 10/2005, which establishes the core legal and regulatory framework for procurement, and ten additional decree laws that directly or indirectly modify the provisions of the original law.⁷ The current legal framework is confusing and lacks internal consistency. The National Procurement Directorate of the MOF served as the overall regulatory body for procurement but was dissolved in 2012; there is currently no body with overall authority to regulate procurement. The government has prepared an omnibus procurement law that would address these inconsistencies by strengthening the legal framework and establishing a new regulatory body.

7. Procurement responsibilities are currently divided between the line ministries (for contracts below $1 million) and the NPC (for contracts above $1 million). The Infrastructure Fund (IF) was established in 2011 for financing and administration of capital projects valued above $1 million. The IF’s Administrative Council is the executive body that manages the IF. Establishment of the IF involved the following changes in procurement processes: (i) line ministries retained responsibility for project proposals, but overall responsibility for managing procurement processes shifted to the NPC; and (ii) the major projects secretariat was given responsibility for analysis of project proposals and presentation of projects to the Budget Review Committee and the IF’s Administrative Council.

8. The Procurement Legal Regime mandates the use of competitive procurement, but the use of less competitive procurement instruments (such as single sourcing and use of quotations) is prevalent. The use of exceptions to the Procurement Legal Regime is not always justified, and mechanisms for holding public officials accountable for results are not well developed. Service delivery is hampered by poor linkages between financial programming and procurement planning, and ineffective internal auditing in personnel and procurement management. There is considerable potential to strengthen procurement practices to achieve a balance between risk and accountability while ensuring transparency and efficiency.

D. **Anticorruption**

9. Since independence in 2002, the government has sought to establish a robust legal and institutional framework to prevent corruption. The Office of the Inspector General was established in 2000 to oversee the use of government resources, and the Office of the Provedor for Human Rights and Justice was given initial responsibility for some anticorruption activities. These responsibilities were subsequently transferred to the ACC. The ACC is responsible for

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corruption prevention, education, and investigation. The ACC does not have prosecutorial authority and needs to work closely with the Office of the Prosecutor General. While key institutions are now in place, their independence needs to be assured, they need to be resourced effectively, and their roles need to be consolidated. Timor-Leste was ranked 123 of 168 countries in the 2015 Transparency International Corruptions Perception Index.

### Table 2: Risk Management Plan

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<th>Risks</th>
<th>Risk Mitigation Actions</th>
<th>Indicators</th>
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<tr>
<td><strong>Budgeting.</strong> (i) weak budget forecasting undermines O&amp;M and threatens sustainability, (ii) weak public financial management capacity in line agencies, undermines efficiency, (iii) weak internal auditing threatens integrity.</td>
<td>ADB will (i) help to build line ministries’ capacity for sector and project-level budgeting, including capital and O&amp;M expenditure, (ii) enhance public financial management systems for internal audit, (iii) create ring-fenced O&amp;M budgets, and (iv) enhance PPP as a modality.</td>
<td>Increased sector O&amp;M budgets; improved quality of internal audits; increased consideration and use of PPP modalities; reduction in unplanned expenditures</td>
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<td><strong>Accounting and reporting.</strong> Most PMUs and PIUs have poor organizational structure, limited staff capacities, and weak systems for financial management of projects.</td>
<td>For all ADB-funded projects, (i) financial management units will be created inside each PMU or PIU; (ii) financial management unit staff will complete training on International Public Sector Accounting Standards; (iii) financial management units will prepare a comprehensive project financial management manuals; (iv) PMUs and PIUs will create specific communication and reporting plans.</td>
<td>Financial management units created inside all ADB project PMUs and PIUs, and financial management reports submitted in a timely manner</td>
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<td><strong>External audit.</strong> The absence of a supreme audit institution and limited number of independent first-tier audit companies contributes to significant delays to audit of annual project financial statements.</td>
<td>The government will finalize its road map to create a supreme audit institution. Sufficient budgets and timeline covenants will be incorporated in ADB projects to enable timely engagement of top-tier audit companies.</td>
<td>100% compliance with submission of annual audited project financial statements to ADB and the government by the implementing agencies</td>
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<td><strong>Procurement.</strong> (i) National procurement systems are not fully aligned to international standards; (ii) capacity limitations within agencies responsible for procurement delay project execution and reduce transparency; (iii) additional concerns exist about project management, supervision, and monitoring, as well as the limited, albeit growing, capacity of private sector contractors; (iv) procurement planning (packaging, technical specifications, contracting strategy) and processing are poor.</td>
<td>Country level. A road map for assisting the NPC will be developed with support from ADB and other donors and will include (i) a role definition for the NPC (ii) actions for NPC staff development, (iii) a train-the-trainers program for NPC staff to disseminate procurement skills, (iv) support for enactment of the omnibus procurement law, (v) creation of harmonized procurement guidelines, (vi) introduction of standard bidding documents, (vii) development of appropriate legal provisions for PPP procurement, and (viii) implementation of procurement systems.</td>
<td>Country level. Omnibus procurement law is adopted; standard bidding documents and PPP guidelines are issued by the NPC; procurement oversight system is established; capacity building for e-procurement completed</td>
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<td><strong>Corruption.</strong> There are only a few anticorruption provisions for procurement, and there is no complaints review mechanism to handle alleged breaches of the Procurement Legal Regime.</td>
<td>ADB will work with other development partners to support introduction of an independent complaints review mechanism. ADB will also increase its oversight of procurement and financial control.</td>
<td>Complaints review mechanism operational</td>
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</table>

ADB = Asian Development Bank, MOF = Ministry of Finance, NPC = National Procurement Commission, O&M = operation and maintenance, PIU = project implementation unit; PMU = project management unit, PPP = public–private partnership.

Source: Asian Development Bank

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