



**GOVERNMENT OF  
THE DEMOCRATIC REPUBLIC OF TIMOR-LESTE**

**REVIEW OF DISCRETIONARY GRANTS  
AND OTHER KEY AREAS**

May 2008

One of three reports comprising the Review of Key Activities  
Contract No: RDTL - 81197

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## 1.0 EXECUTIVE SUMMARY

### 1.1 BACKGROUND

The 4<sup>th</sup> Constitutional Government of Timor-Leste was inaugurated on 14<sup>th</sup> August 2007. Since that time, the Government has been putting in place its structures, systems and processes to establish a working Government for the next term. Part of this effort has been learning of the structures, processes and operations of the previous Government. The purpose of the review is to assist the ongoing development of open, transparent and accountable Government by providing the following information in regard to nominated key areas:

- The systems, processes and practices that govern certain key areas and activities of Government;
- The adequacy of the number and capacity of currently assigned human resources including both international advisors and national staff;
- The controls required to ensure integrity of these programs and the degree to which these already exist and are effective;
- The steps that are required to fix anomalies and deficiencies in the controls, systems and processes, and
- Identification of areas in which the operation of controls would suggest that the government has a significant exposure (potential or current) to inefficiencies, fraud and corruption.

The areas reviewed were nominated by the Minister of Finance and included:

- The Solidarity Fund (*Ministry of Labour and Solidarity*; \$5m)
- The Community Grants Fund (*Ministry of Agriculture, Forestry and Fishing*; \$4.8m, *social activity grants under Prime Minister's Office*; \$1m)
- Local Development Program (*Ministry for State Administration*; \$342k)
- School meals and equipment (*Ministry of Education and Culture*; \$2.2m)
- Contingency Reserve (*Ministry of Finance*; \$3m)
- Infrastructure (*Ministry of Transport and Communication*)
- National Police of Timor-Leste (PNTL)

The reviews of Infrastructure and PNTL resulted from a special request by the Minister of Finance to include these areas in place of the Veterans Fund (Ministry of Labour and Solidarity, and the Compensation for damage and loss in the Crisis Fund (Ministry of Labor and Solidarity).

A copy of the original full terms of reference is presented in Appendix A while Appendix B presents our own statement of liability in relation to this work.

## 1.2 APPROACH

Our approach to this review entailed interviewing key stakeholders to obtain their perspectives on process efficiency, documenting the system and examining specific instances of transactions or events that have occurred in the process.

Our approach involved five phases.

- defining the key elements of the process for each nominated area
- documenting the activities performed for each of these elements
- identifying the risks of systemic deficiencies and opportunities to commit fraud
- reviewing in greater detail specific instances of suspected fraud or control breakdown
- developing recommendations for improvement.

### 1.3 SUMMARY OF KEY FINDINGS

- Significant amounts of public grant funds budgeted for the fiscal year 2006/07 have been carried over into the Transition Budget period. Of the \$13.8 million allocated for the grant programs reviewed, it is estimated that \$3.5 million remains undistributed to the community at December 2007.

Legislative requirements dictate that to the extent that appropriations are not required to pay for goods or services ordered or received at 30 June, such appropriations lapse at that date. In practice, however Ministries have continued to issue Commitment and Payment Vouchers to the Ministry of Finance calling on 2006/07 public grant funds. We understand that the Minister of Finance has recently clarified the situation with Ministries.

- Ministries were found to be exposed to both **systemic risks** (the risk of ineffective or inefficient procedures) as well as the **risk of fraud** throughout various elements of public grant funds as well as some of the other key areas reviewed, including Infrastructure and the National Police of Timor-Leste.

With respect to public grant funds, systemic issues have led to the significant carry over position of many of the grant programs. In particular, limited strategic management, limited governance frameworks and lack of trained resources have contributed to the carry over position.

When asked, only the Ministry of Agriculture, Forestry and Fishing was able to identify and discuss cases of alleged misappropriation of funds. There were relatively few instances of fraudulent practice noted by Ministry personnel as having occurred or having been investigated despite clear exposure of some procedures within the public grant processes to significant risk of misappropriation and fraud.

The lack of any fraud or error having been noted for investigation by Directors of Finance or program administrators may be indicative of the lack of resources and capacity available within each Ministry to measure and monitor these programs in an effective manner progressively throughout the year.

- The grant programs and other high risk areas identified by the Government face some unique challenges, which reflect some unique capacity constraints within Timor-Leste. In particular, cash is a highly liquid commodity and cash handling practices are insecure and risky, but usually necessary in the environment of a developing country such as Timor-Leste.

These unique constraints can make it very difficult for the distribution of grant funds to reach their intended purpose in a timely and efficient manner, or even at all and have also been exposing administration staff to security risk.

- Converse to the trend of carrying over funds with public grants, levels of expenditure within the Contingency Reserve have escalated in 2006/07 compared with 2005/06. In 2006/07, expenditure was \$2.6 million compared with \$525,000 in the previous year.

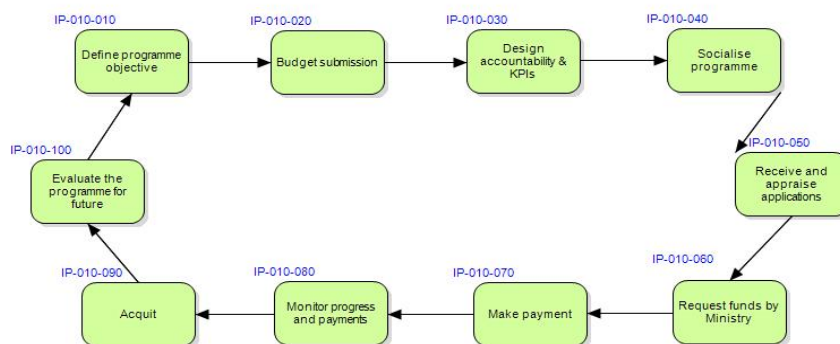
The reserve has been largely used for urgent and unforeseen expenditure. Contributing to much of this increase were events such as the need for a major rice shipment during the rice crisis throughout Asia during March 2007, significant financial consequences of some poor contract management and, although not unforeseen, preparatory costs associated with the 2007 elections. No direct fraudulent practices were evident, however there were some inconsistencies and inadequacies in the documentation attached to payment authorisation documents, in particular the rice shipment.

- With regard to findings from enquiries made with the National Police of Timor-Leste (PNTL), it would appear that the newly centralised Finance Unit, and in particular the finance procedures conducted by the Cabinet of Inspection are operating effectively. It is confirmed that transactions exhibiting indicators of fraudulent activity have been identified by the Cabinet of Inspection. Preliminary investigations into such transactions have been associated primarily with procurement activities for the PNTL.

It is of the view of the Cabinet of Inspection that the framework by which indicative fraudulent practices should be reviewed, pursued and prosecuted be strengthened by way of co-ordinating an anti-corruption monitoring approach with other organisations in the community guided and supported by strong government leadership.

**Risk Profile of Discretionary Grant Programs:** For each discretionary grant program, elements of systemic risk and fraud risk were identified. A preliminary assessment of the complexity of implementation of measures required to address these broad categories of risk were also documented. Risk profiles have been outlined at Section 1.

**Discretionary Grant Processes:** Although each program has a number of unique processes, our initial review of discretionary grant programs across Government determined ten generally common process elements. These have been summarised in the diagram below.



Key tasks falling under each of the above key process elements were documented.

This review did not examine each grant program in detail but it does provide reasonable insights in process integrity, the risk of fraud and the complexity of opportunities to address systemic weaknesses across Government grant funding processes more generally. The report attempts to provide a balanced perspective of grant funding operations by offering comment on the strengths and weaknesses of key risks, controls and sub processes that would generally be expected to be in place throughout any government grant administration. We consider that the identified risks, controls and recommendations are appropriate to the context of a developing country such as Timor Leste.

Section 2 of this report provides details of all of the risks and issues identified during the review and, where appropriate, is illustrated by examples of specific transactions or events that have actually occurred within the process.

**Other key areas:** Our Terms of Reference included a review of some additional areas unrelated to grant funding – the Contingency Reserve, Ministry of Infrastructure (IGE) and PNTL. Key findings have been outlined within Section 1 and 3 of this report.

## 2.0 RISK PROFILE OF EACH AREA REVIEWED

### 2.1 SOLIDARITY FUND

The Solidarity Fund exists to provide financial assistance to those suffering from the military crisis, such as ex-military and vulnerable groups. Appropriation for the 2006/07 year amounted to \$6.5 million. The identified risk profile is summarised in the table and narrative below.

	Systemic risk	Risk of fraud	Complexity to address
People and Training	H	M	L
Strategic Management	H	M	M
Policy & Guidelines	L	L	L
Use of technology	L	M	M
Communication & Reporting	M	M	L
Governance	L	L	L
Legislative framework	L	L	L

**People & Training:** For the purpose of administering this fund, the Ministry of Labour and Solidarity effectively takes on the role of a small banking institution from which cash withdrawals are made to assist the community in crisis. Administration staff have no finance or accounting training and rely wholly on their cumulative experience. Aside from the Director of Finance & Administration, only two finance and administration personnel administer the \$5 million cash flow.

**Strategic Management:**

- These very limited staff numbers are likely to become significantly overwhelmed in the event of a crisis attempting to accurately account for immediate cash distributions.
- Moreover, despite the significant cash holdings on premises, the building location is not built as would be expected of a financial institution. It is recommended that:
  - a) the Ministry of Labour & Solidarity not be used as a banking institution, but to evidence authorisation of distributions to be made to the community from a major banking institution (eg BNU);
  - b) in the meantime, a contingency plan should be developed for additional resources and security measures in the event of a crisis.
- There were 18 different initiatives funded through the Solidarity Fund in 2006/07. There may be a degree of duplication in providing funds through the Solidarity Fund to the extent that the Fund's objectives and its recipients overlap with other funding sources. For example, ex-military, veterans and vulnerable groups may overlap with other Ministries such as the Ministries of Defence and Health if not continually co-ordinated.

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**Policy & Guidelines:** Ministerial Despatch of 19 December 2006 outlines the objectives, priorities and criteria for the Solidarity Fund. No significant issues to note.

**Use of Technology:** Accounting records (debits and credits) are kept in Microsoft Excel and the safe is maintained in a relatively insecure environment. Excel documents can be readily modified and combined with access to the safe, the Solidarity Fund is exposed to a moderate level of fraud risk.

**Communication & Reporting:** No proforma proposal applications are used by the community to apply for funding to the Ministry.

There are some good communication and reporting practices such as:

- The Ministry of Labour & Solidarity compare personnel records of the military with those of the Ministry of Defence. This is a systemic strength, however should be conducted periodically to ensure deceased individuals or those moved offshore do not continue to have payments claimed.
- Accounting records were generally well kept. A report detailing each program funded by the Solidarity Fund was made available which provided total budgeted expenditure, expenditure committed and requested via CPV, cash distributed to the community and the residual bank balance for each program reconciled to cash holdings in the safe. According to the report, of the \$6.5 million revised and approved budget for the Solidarity Fund in fiscal year 2006/07, \$5.2 million had been committed with CPV, \$4.9 million had been received from the Ministry of Finance of which \$4.7 million had been physically distributed at 23 November 2007. This leaves \$1.25 million of the 2006/07 budget remaining uncommitted at November 2007.
- Daily cash reconciliations are performed and overseen by the Director of Finance & Administration.

**Governance:** No issues noted.

**Legislative Framework:** Crisis assistance is governed by Government Resolution December 9 / 2006. No significant issues of note.

## 2.2 COMMUNITY DEVELOPMENT FUND

The Community Development Fund was established to reduce poverty by supporting farmer groups develop self-sustainable agricultural activities in rural areas. Appropriation for the 2006/07 year amounted to \$4.8 million. The identified risk profile is summarised in the table and narrative below.

	Systemic risk	Risk of fraud	Complexity to address
People and Training	M	L	M
Strategic Management	M	L	L
Policy & Guidelines	L	L	L
Use of technology	L	L	L
Communication & Reporting	H	H	M
Governance	L	H	M
Legislative framework	L	L	L

### People & Training:

- There has been a lack of resources to assist the execution of the Community Development Fund. For example, of the 442 Suco's at the date of our review there had been only 71 facilitators approved by the Ministry of Agriculture, Forestry and Fishing (MoAFF). Successful execution of the grant programs within each Suco is highly dependent upon assistance from a local facilitator.
- Staff within the Finance and Administration function have not had any formal finance or accounting training.

### Strategic Management:

- Success of the community grant program is dependent on each facilitator having the appropriate agricultural background (for example, experience to operate machinery) however the funding objectives do not focus significantly on any capacity building for the agricultural skills of facilitators.
- The Community Development Fund promotes the establishment of sustainable, income-generating agricultural activities.
- Grant funding has appropriately taken into account a 5% contingency amount to cover costs of administering the fund.
- In the fiscal year 2007/08, the Ministry of Agriculture wishes to focus the grant funding to areas that shall promote great potential for the agricultural product of the country.

**Policy & Guidelines:** Policies and guidelines have been documented within the recently compiled Community Fund Development Report (FDC). Proforma and example documentation has been included within the publication. No significant issues of note.

**Use of technology:** There is presently only limited capacity for funds to be distributed to districts by bank transfer, risking the security of administrative staff in transporting cash funds to the districts themselves.

**Communication & Reporting:**

- Direct communication is made with the districts and related Sucos by socialising the program, its processes and requirements via 1 day on-site workshops.
- Physical monitoring of the agricultural activity vests with the district staff member of the MoAFF and the facilitator of each Suco. Although photographic evidence is provided to the MoAFF in Dili, there is a risk that over time staff will integrate with the community, independence will erode and reporting to the Ministry could be at risk of misrepresentation.

The Community Development Program may benefit in the future from a rotation of district staff members between districts or alternatively a central monitoring program administered from Dili covering areas of most risk.

- There is no specific format of acquittal reporting to the Ministry. A proforma outline would assist each Suco in articulating their business case for their next tranche of funding and likewise assist the Ministry in an objective and efficient evaluation process. The evaluation prior to release of the additional 60% funding is otherwise largely an exercise of judgement.
- The recently compiled Community Development Fund Report is an example of good transparency.
- There have been cases reported of misspent funds that have been or are in the process of being investigated.

**Governance:** In July 2006 there was no framework by which to administer the Community Development Fund. As a result, and despite a budget allocation of \$4.787 million at the beginning of 2006/07, the first distribution of cash was not made to the district regions until 2 May 2007.

Significant funds from the 2006/07 Budget have been carried over. Records of the Ministry indicate that at December 2007, \$3.4 million has been received and distributed with \$1.4 million still to be distributed.

International advisors conducted a review to design a framework for the grant fund process. However, the Ministry of Agriculture assessed the proposal as too difficult to implement within the Timor-Leste environment and so designed and adopted their own framework.

The framework appears sound with one key exception highlighted as follows:

- The fund is significantly dependent and therefore exposed to the capacity and integrity of the district staff members and Suco facilitators.
- There is no segregation of duties between those responsible for monitoring activities and custody of the cash. Locally based staff and facilitators receive, expend and acquit all cash proceeds in addition to the responsibility for monitoring progress of projects at each Suco. Despite staff members of each district being appointed and employed by the MoAFF, there is a risk over time that the staff member's independence from the Suco will erode.

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- Otherwise, the framework has some strong features as follows:
- Appraisal of applications is conducted by two separate commissions – Technical Commission (MoAFF) and the Finance Commission (Ministry of Finance);
- Three representatives from each Suco are to be nominated to supervise activities;
- 60% of grant funds are withheld until the first tranche of expenditure is demonstrated to the District Staff Member as having been spent appropriately;
- The community grant programs are well socialised with the community via a 1 day workshop between the Ministry of Agriculture and the relevant district and suco members.

**Legislative Framework:** Decree Laws have been established and are referred to throughout the proforma community grant documentation. No significant issues of note.

### 2.3 LOCAL DEVELOPMENT PROGRAM

The purpose of the Solidarity Fund is to fund the establishment of an institutional and procedural framework, sub-national government institutions (assemblies), local level planning, local level finance management, local level procurement, local level capacity building and to establish channels for interactions between local government and community structures.

Appropriation for the 2006/07 year amounted to \$342,000. The identified risk profile is summarised in the table and narrative below.

	Systemic risk	Risk of fraud	Complexity to address
People and Training	M	L	L
Strategic Management	M	L	L
Policy & Guidelines	L	L	L
Use of technology	L	L	L
Communication & Reporting	H	H	M
Governance	L	L	L
Legislative framework	L	L	L

**People and Training:** Training has been provided for State Administration staff to perform their tasks, however no job manuals exist.

**Strategic Management:** Instances of good strategic management include:

- The Local Development Program (LDP) has been established in a staged manner. Bobonaro and Lautem districts were selected for pilot purposes.
- Local tender boards are expected to be established to procure up to \$10,000 at the local level.
- Other Ministries are represented as part of the District Assembly and Sub-district Assemblies.

Areas of strategic management in need of improvement include:

- The basis for budget submissions. The Budget submission to the Ministry of Finance for 2006/07 was based on population statistics from the 2004 Census.
- The 2008 strategic planning process may lead to a delay in the distribution of funds. It was represented to us that plans to expend the fiscal year 2008 Budget allocation are expected to be completed by May 2008, after which it is expected to be a further six months before expenditure proposals are submitted and approved before a CPV can be raised. Consequently it may be some 11 months before funds are distributed to local districts from the 2008 Budget allocation. This would appear to be an unreasonable time lag. Of the \$342,000 Budget allocated in 2006/07, only \$201,000 has been distributed at the date of this report, with \$154,000 committed.

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**Policy and Guidelines:** A comprehensive Institutional and Procedural Framework exists including Ministerial Decrees and Regulations to provide guidance regarding district and sub-district planning and implementation guidance, finance and procurement procedures.

**Use of technology:** No significant issues.

**Communication & Reporting:** District and Sub-district Assemblies are required to prepare monthly expenditure reports to the District Administration Treasury, which should be forwarded to the Ministry of State Administration. However, there have been instances of untimely reports impacting the effectiveness of the monitoring of the LDP. District Finance Officers are not dedicated LDP personnel. Consequently, the needs of the LDP are not necessarily a priority when busy. In particular, invoices for recurrent expenditures remain outstanding.

**Governance:** District Assemblies and Sub-district Assemblies for the piloted regions were established in 2005 and 2006. Both assemblies have voting members from each relevant Suco as well as non-voting members from other Ministries. No significant issues of note.

**Legislative Framework:** Ministerial Decree Law regarding Local Assemblies and eight separate Regulations were established in 2005. No significant issues of note.

## 2.4 SCHOOL MEALS AND EQUIPMENT GRANTS

The purpose of the school meals and equipment grants program is to promote good nutrition and encourage students to go to school.

Appropriation for the 2006/07 year amounted to \$2.2 million. The identified risk profile is summarised in the table and narrative below.

	Systemic risk	Risk of fraud	Complexity to address
People and Training	H	M	M
Strategic Management	H	H	L
Policy & Guidelines	L	L	L
Use of technology	H	H	L
Communication & Reporting	H	H	L
Governance	H	H	M
Legislative framework	L	L	L

### People & Training:

- The school feeding program has only recently commenced operation, is reportedly under-resourced with insufficient training to administer the significant budget in 2006/07.  
It was represented to the audit team by the program administrator that there are only 3 people dedicated to the School Meals and Equipment Program across six schools, including one driver. The apparent lack of strategic resourcing for this large fund appears to be hampering the administration of the fund, including food and utensil deliveries as well as the quality of accounting records.
- It was also reported that there have been cases where food has been procured in Dili requiring transport and delivery to various schools for which the Ministry has had to rely on the availability of miscellaneous staff from other departments within the Ministry of Education and Culture to drive the delivery.
- In cases where all staff have been busy, food deliveries have reportedly had to be cancelled. There were no specific accounting records to validate these representations however.
- No training has been provided to finance and administration staff except to the previous program manager who attended one week's technical training organised by the World Food Program in a previous year.
- No effective or efficient filing system for key documentation is maintained. Accounting records were not made available despite a request for a list of grant funds expended to be made available.

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**Strategic Management:** Despite the joint drafting the school Nutrition Plan between the Ministry of Health and Ministry of Education and Culture in September 2005, there appears to have been a lack of strategic management evidenced by:

- A significant delay in the commencement of the School Feeding Program within the Ministry of Education and Culture. Despite a Budget allocation of \$1.4 million at the commencement of 2006/07, the program has only commenced in April 2007. The Ministry of Education and Culture states that lengthy discussions were held with the Ministry of Finance regarding a need to amend program activities subsequent to the allocation of the Budget. The nature of items to be purchased with grant funds had to be renegotiated (ie food acquisitions were extended to include cooking utensils).

The scope of the grant program at the Budget planning stage is fundamental to a successful strategic outcome.

- The scarcity of resources assigned to the program has necessitated the use of staff from other departments at short notice to oversee the delivery of goods. Where staff are unavailable, deliveries are reportedly cancelled.
- At no stage is a school representative, such as a school Principal required to directly evidence by way of signature the physical volume of food or utensils received. This is assumed to be the role of the District Administrator rather than the ultimate beneficiary.
- There is a high level of cash handled by the Ministry of Education for the purchase of food items other than rice. Cash reconciliations to account for the contents of the safe are not conducted on a daily basis. Accordingly, a misappropriation of funds from the safe may remain undetected for a period of time.

**Policy & Guidelines:** Formally documented Implementation Plans and Guidelines have been established.

**Use of technology:** No specific issues of note, however record keeping could benefit from better application of technology.

**Communication & Reporting:** Record keeping is very poor. No effective audit trail exists to verify the quantities of goods delivered, or payments received and expended.

Upon the audit team's request to disclose the amount of funding that had been expended to date, it was necessary for the amount to be derived manually by the grant program and finance teams.

According to manual records of the Ministry of Education and Culture, of total grant funding of \$1.4 million for the 2006/07 fiscal year, total expenditure to December 2007 equates to approximately \$496k, leaving unspent funds of approximately \$904k.

**Governance:** Given the limited resources and issues regarding strategic management of the 2006/07 Budget, there does not appear to be any effective governance framework.

**Legislative framework:** No issues noted.

## 2.5 HEAVY EQUIPMENT MANAGEMENT INSTITUTION (IGE)

The operations of the Heavy Equipment Management Institution (IGE), a government business division of the Ministry of Infrastructure, was created to support public work activities, small community infrastructure needs and to support government needs.

IGE does not receive public grant funds from the government but instead derives its main revenue from equipment and vehicle rentals.

The identified risk profile is summarised in the table and narrative below.

	Systemic risk	Risk of fraud	Complexity to address
People and Training	H	M	L
Strategic Management	H	H	M
Policy & Guidelines	H	H	M
Use of technology	M	L	L
Communication & Reporting	M	M	L
Governance	H	H	M
Legislative framework	H	H	M

**People and Training:** There has been a general lack of training for usage of specialised equipment, project management skills and language skills.

There has also been a lack of training to assign staff to a supervisory role in order to monitor the fieldwork.

**Strategic Management:** Incomplete governance and legislative frameworks are indicative of a lack of effective strategic management of the IGE operations.

### Policy & Guidelines

- Policies practiced require that within 5 days from the date the equipment or vehicle is used, the contractor must pay 40% of the estimated costs to IGE by way of bank transfer. The contractor is required to present a bank statement evidencing that the 40% has been paid. Bank statements presented for our review were not documents issued by the banking institution, but deposit slips on IGE letterhead exhibiting a stamp from the bank.
- The remaining 60% is typically paid in cash to IGE in order to pay contractors and fuel costs. Any residual cash is held within IGE's safe on premises and reportedly used for maintenance of equipment and small public works.

Accounting for infrastructure contracts can be complex. Without adequate finance and accounting training for staff, the risk of error and fraud is heightened.

- A detailed register of equipment and related movements is well kept.

**Use of technology:** Training in the use of specialised technical equipment on site is needed.

**Communication and Reporting:** Without any effective governance or organic laws, reports are likely to be ineffective. Comprehensive reports on a monthly basis for each contract detailing money received, yet to be received, stage of completion of contracts and costs to date should be prepared and separately monitored.

### **Governance**

- There have reportedly been complaints from contractors regarding the inequitable nature of tenders awarded through the Ministry of Finance.
- The Deputy Director of IGE has a view that there is a need for better monitoring of the IGE operations, its contracts as well as the service levels of contractors.

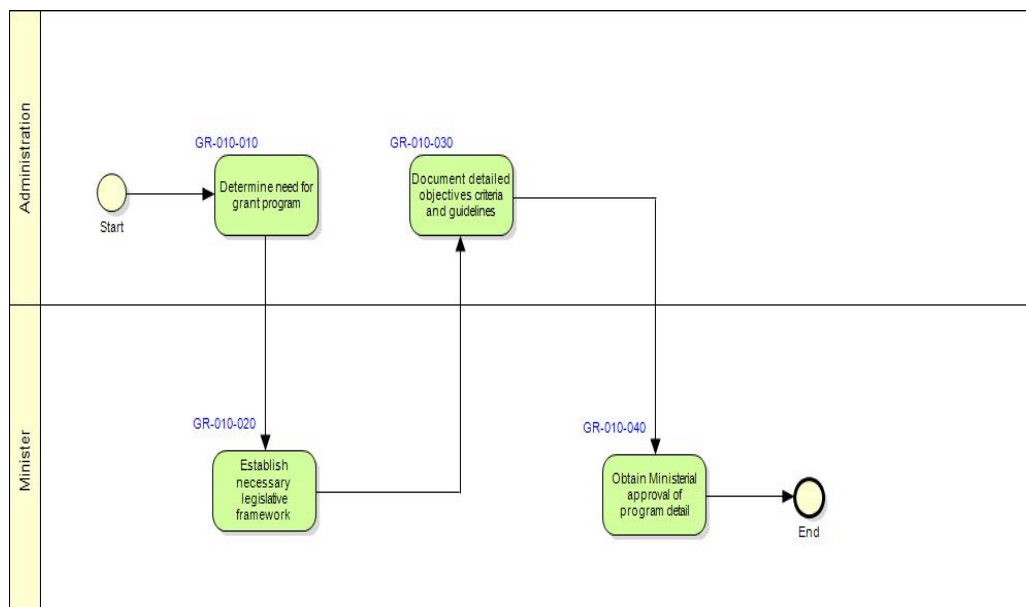
### **Legislative Framework**

- There is no separate legislation specific to IGE's operations to govern activities or clearly define its objectives. In particular, there is no Organic Law for the operations of IGE. Lack of Organic Law is seen by the Deputy Director of IGE as impacting productivity of the employees where from time to time employees will refuse to accept tasks as they are not sure of their roles and responsibilities.
- Agreements between IGE and relevant construction contractors are written by the Director of IGE and Deputy Director of IGE without professional legal assistance. It is the expectation of IGE (and apparently the practice) that onus is on the contractor to meet any cost overruns. Upon review of an example of such an agreement, however we determined that the requirement that excess costs be met by the contractor were not specified in the agreement leading to financial exposure of the government.

### 3.0 PROCEDURAL FINDINGS AND OBSERVATIONS

#### 3.1 DEFINE PROGRAM OBJECTIVES AND DEVELOP PROGRAM GUIDELINES

Public grant programs should operate with clearly defined and documented operational objectives. These objectives should in turn align with the strategic objectives of each Ministry. Once clearly documented, the objectives should be approved by the relevant Minister. Program guidelines should then be developed for the purpose of assisting the implementation, execution and achievement of the program objectives. A summary of the process that should be in place is presented below:



A summary of risks and issues identified within this sub process are as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	School Meals and equipment grants	Community Grants
<b>Control weakness/risk</b>	<b>Likelihood of control weakness</b>				
Duplicate funding	L	H	M	M	H
Program objectives not clearly defined	L	L	L	L	L
Program objectives not authorised	L	L	L	L	L

**Duplicate funding:** There is a risk that grant recipients may be able to obtain grant funding for the same purpose or program objective from more than one Ministry. Duplicate funds for the same or similar objectives may be provided to common beneficiaries where some Ministerial public funding strategies overlap. No mapping of relationships with other funding sources across government was provided. This may also have an impact on economies of scale where there is an opportunity for technical knowledge to possibly be better shared and co-ordinated between Ministries.

In addition, there was no immediate evidence to indicate that public grant programs across all Ministries are comprehensively reviewed for the purpose of identifying any possible conflicting objectives between Ministries.

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*Example: Co-ordination between Local Development Program other Ministries*

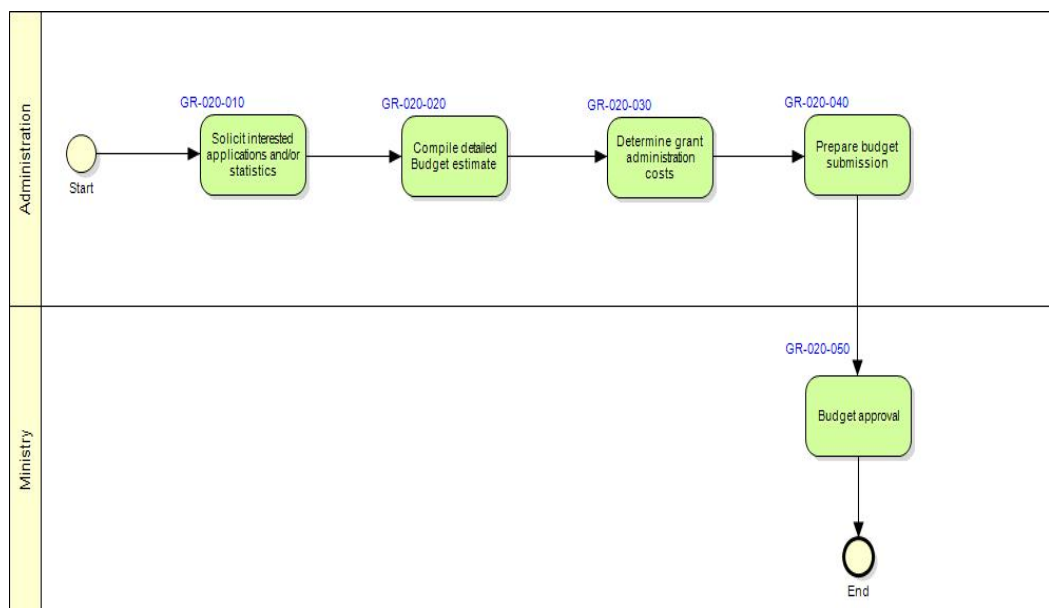
*As an example, the Ministry of State Administration provides 15% and 41% of the LDP funding for the purpose of agricultural and education activities respectively, at the local level. Likewise, the Ministry of Agriculture provides funds to Suco's for agricultural activity in rural areas and the Ministry of Education provides School Feeding and School Grants Programs to all districts.*

*Ministries, including the Ministry of Agriculture and the Ministry of Education each have one non-voting member appointed to the LDP sub-district assembly, however reliance on these appointments to co-ordinate funding across their respective Ministries in such a way to ensure there is no duplication of funds to common beneficiaries for similar projects is not always practical nor sustainable where there will inevitably be a turnover of appointments to the sub-district assemblies.*

**Program objectives not clearly defined:** Many of the Ministries associated with the above public grant funding were able to articulate each of their program objectives and make reference to authorised and documented program objectives that were reasonably clear.

**Program objectives not authorised:** In each of the above cases, program objectives and/or relevant legislation had been approved.

### 3.2 BUDGET AND SUBMISSION



A summary of risks and issues identified within this sub process is as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	School Meals and equipment grants	Community Grants
<b>Control weakness/risk</b>	<b>Likelihood of control weakness</b>				
Outdated budget submissions	L	H	L	M	L
Operating costs not identified	L	L	H	H	L

**Unsound budget submissions:** Where inaccurate or outdated information is used as the basis of a business case for the budget submissions provided to the Ministry of Finance for public grant funds, allocation of public funds between Ministries may become ineffective.

*Example: LDP population statistics*

*LDP funding for fiscal year 2006/07 was based on population statistics from the 2004 Census. Population statistics at the date funds are distributed will possibly be significantly different to those of 2004, particularly where residents have been internally displaced since that time.*

**Operating costs not identified:** Although the main costs of a grant program are the funds paid to the public, there are also costs related to the administrative support for the program to be taken into account when estimating budget requirements. Budgeting for administration costs is essential to the success of each program.

There was no significant evidence to indicate that administration costs that would be directly associated with the operation of the Solidarity Fund or the School Meals Programs were adequately budgeted for as part of the overall program funding from the Ministry of Finance. Conversely, the Ministry of Agriculture has documented anticipated administrative expenditure in detail.

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*Example: 5% Contingency Amount*

*The Ministry of Agriculture outlines a 5% contingency amount built into the budgeted grant spend for the purpose of covering administration costs for the implementation of the program. Such costs are itemised with amounts set aside for payments to rural facilitators, leaflets, transport of residents to and from their Suco, fuel and computer equipment.*

The contingency amount should be capped to a limit and/or a process be developed to ensure the continued measurement and accountability for such contingency amounts on a regular basis in order to deter and limit any misappropriation or fraudulent spending of the contingency.

### 3.3 DESIGN PROGRAM ACCOUNTABILITY AND KEY PERFORMANCE INDICATORS (KPIS)

This is an element within the grant funding processes having the potential to greatly limit the susceptibility of the government to the risk of continuing to fund ineffective programs as well as limiting the risk of fraud. Each of the grant funds reviewed were identified as having some exposure here.

It is the responsibility of each Ministry to ensure that accountability is developed at the beginning of each program in a way that accurately reflects the desired operation and outcomes of each approved activity.

Without measurable, consistent and timely accountability to the Ministry of Finance for public grant funds, combined with a lack of definition in roles and responsibilities of those administering the grant programs, there is significant room for funding abuse, misappropriation or fraud of grant money.

A summary of risks and issues identified within this sub process is as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	School Meals and equipment grants	Community Grants
<b>Control weakness/risk</b>	<b>Likelihood of control weakness</b>				
Roles and responsibilities not defined	H	M	M	M	M
Lack of financial delegations	H	L	L	L	L
No reporting mechanisms	H	H	H	H	H
No performance measures	H	H	H	H	H
No fraud control plan	H	H	H	H	H

**Roles and responsibilities not defined:** Generally, the roles and responsibilities of stakeholders such as various evaluation committees or local facilitators have had their roles and responsibilities formally documented, however administrative staff within each Ministry such as finance and administration personnel were found less likely to have had their roles and responsibilities in relation to administering these grant programs detailed in a clear and formal manner.

The lack of job description at the operational level may explain, in part, a lack of accountability and inaction in some areas.

*Example: Lag in monthly reporting*

*Monthly reporting of the LDP program to the Ministry of State Administration from the District Finance Officers in acquitting recurrent expenditures on a regular basis has a back log, in part due to the fact that the requirement of the District Finance Officers to report to the Ministry of State Administration on such items of expenditure compete with their roles and responsibilities to other Ministries on a monthly basis and so is not necessarily a priority task.*

*Example: Responsibility for monitoring and controlling budgeted spend*

*When asked directly, some of the Ministries considered the responsibility for monitoring the over or under expenditure of the grant program funding against budget at a detailed level to be that of the Ministry of Finance rather than the responsibility of their own Ministry.*

**Lack of financial delegations:** Generally, financial delegations of authority to a range of staff commensurate with levels of responsibility were evident. No significant issue regarding financial delegations.

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**No reporting mechanisms:** It is important that each Ministry report regularly to the Ministry of Finance on its use of program funds. There was neither evidence of a consistent format nor regularity of reporting by each Ministry of its public grant expenditure to the Ministry of Finance.

**No performance measures:** A performance management framework is essential for both the program administrators within each Ministry and for the Ministry of Finance to assess the effectiveness of these large discretionary grant programs.

For the purpose of accountability, it is important to link key performance measures to each operational objective of the grant program. Difficulty in determining key performance measures within the original budget proposal to the Ministry of Finance may reflect an underlying uncertainty as to the purpose of the program activity prior to approval of initial funding.

The Ministry of Finance and grant administrators within each Ministry should design their programs for accountability with regard to both input measures and output measures such as:

Input measures (examples only)	Output measures (examples only)
<ul style="list-style-type: none"><li>• Costs of administering the project to date</li><li>• Number of resources assigned to administering the program</li><li>• Number of training sessions provided to staff</li></ul>	<ul style="list-style-type: none"><li>• Percentage of budget expended</li><li>• Number of completed rural/district projects</li><li>• Number of Sucos visited</li><li>• Number of school deliveries</li><li>• Improved nutrition measures</li><li>• Number of new applicants</li><li>• Number and value of grants awarded</li></ul>

**No fraud control plan:** Ministry personnel were not aware of any fraud control plan nor communication mechanisms in the event that a fraudulent act were discovered. The appropriate procedures are not known to personnel administering the grant programs should they identify any fraudulent exploitation of the grant funds.

### 3.4 SOCIALISE THE PROGRAM

Educating and encouraging as many potential eligible applicants for public grant funds will help the government target available funds toward the most appropriate and deserving funding needs for the country.

Stakeholders should be clearly identified and understood for each grant program. Target groups of stakeholders should be identified consistent with strategic policy outcomes and to ensure the success of the grant program, have adequate time and resources devoted to engaging stakeholders.

A summary of risks and issues identified within this sub process is as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	School Meals and equipment grants	Community Grants
<b>Control weakness/risk</b>	<b>Likelihood of control weakness</b>				
Lack of stakeholder communication	L	L	L	L	L

**Stakeholder communication:** The objectives and operating processes of the grant programs should be communicated to all grant administration staff within each Ministry and potential applicants. Diverse methods of communication should be adopted in order to reach all stakeholders in an appropriate manner whether it be oral, written or visual means.

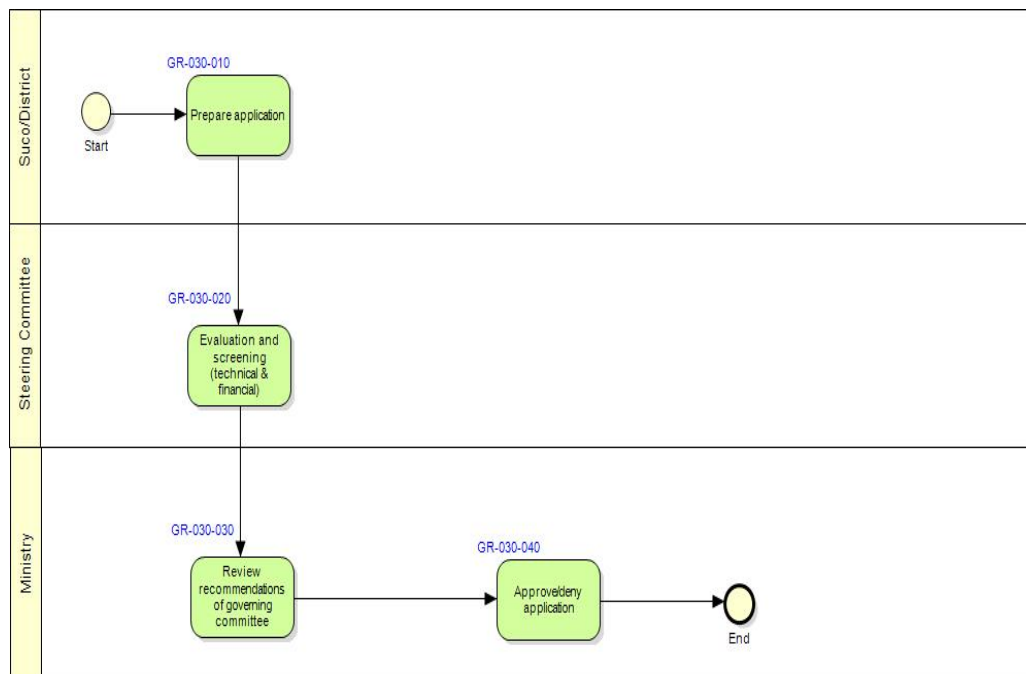
*Example: Ministry of Agriculture – Community Grant Funds*

*The agricultural community grants are communicated via written leaflets as well as verbally via one day workshops conducted on site at each district. This is an example of good, flexible practice in socialising the grant program and broadening the audience of prospective applicants.*

### 3.5 RECEIVE AND APPRAISE APPLICATIONS

The objective of this sub process is to evaluate the credibility of potential beneficiaries and to match the objectives or community needs of the applicant with the identified strategic objectives of the relevant Ministry with respect to the specific program.

This is an element within the government grant funding processes of high susceptibility to fraud. The Solidarity Fund and to some extent the Community Grant funds were identified as having some exposure here.



A summary of risks and issues identified within this sub process is as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	School Meals and equipment grants	Community Grants
<b>Control weakness/risk</b>	<b>Likelihood of control weakness</b>				
Awarding grants to ineligible beneficiaries	H	L	H	L	H
Inequitable treatment	H	L	H	L	L
Lack of transparency	H	L	M	M	L

**Awarding grants to ineligible beneficiaries:** Risk of awarding grants to ineligible individuals or organisations that are not willing or able to complete a community project effectively.

- The Ministry of Agriculture recognises its susceptibility to the fact that there may be unworthy beneficiaries of community grants within some Sucos. To mitigate this, funding is provided in two stages – 40% contribution and a subsequent 60% contribution of funds. This way, should the 40% contribution be abused and minimum requirements not met, no further funding will be forthcoming.

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- The Local Development Program is less susceptible to awarding grant funds to ineligible groups as there are multiple levels of governance overlaying the approval process for each district including the District and Sub-district Assemblies.
- The Ministry of Education is also considered to be relatively low risk in the area of ineligible applicants as grant funds are only awarded to specifically identified public schools co-ordinated with the World Food Program.
- Although there was no direct evidence at the date of the review, there is inherent risk for the Solidarity Fund to be taken advantage of by the community from time to time as a result of its very nature.

### *Example: Ineligible beneficiaries*

*The Solidarity Fund provides payments to ex-military personnel. Such personnel provide their identification at the commencement of the grant funding cycle which are cross-checked by the Ministry of State Administration to the Ministry of Defence records at the time. However there may be a possibility that such individuals move overseas or become deceased while alternative beneficiaries continue to collect payments from the Solidarity Fund on their behalf.*

In addition, the Solidarity Fund does not use any proforma application forms as a design to direct or assist applicants to be considered for fund money. It is unlikely that applicants are providing the necessary information in all cases regarding the appropriate selection criteria to a satisfactory level of information the Ministry of State Administration needs in order to evaluate an application to its full extent prior to approval for funding.

**Awarding grants inequitably between potential beneficiaries:** Each of the grant programs were able to outline criteria used to prioritise different applications.

The risk of individuals or organisations being treated inequitably in the appraisal of applications and awarding of grant funds is considered to be relatively low for most of the Ministries with the exception of the Solidarity Fund.

- The Community Grants within the Ministry of Agriculture provides each Suco with a uniform right to receive \$10,000 with each project application voted on by the community and having to pass through two separate and centrally administered commissions.
- The Ministry of Education lends itself to less bias with its food program funding allocated on a uniform rate per student (by study level).
- The Local Development Program funding allocations are based on population figures.
- For the Solidarity Fund, however, applications are more subjective, without objective and detailed evaluation criteria. Determining whether an activity qualifies as an act associated with the “military crisis” is less objective.

**Lack of transparency and documentation of decisions:** It is considered that there is more transparency and documentation on decisions in relation to the approval or refusal of applications for grants where evaluation committees were established.

### 3.6 REQUEST FUNDS FROM MINISTRY OF FINANCE

Funds are requested via a Commitment and Payment Voucher (CPV) to the Ministry of Finance for the allocation of funds to a particular grant recipient or group of recipients based on previous submissions supporting the budget allocation.

Depending on the particular grant program and the particular beneficiary, funds may be provided in cash from the Ministry of Finance to the relevant Ministry administering the grant program, or where relevant, via cheque to the grant recipient or bank transfer to a district bank branch.

A summary of the risks and issues identified within this sub-process are as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	School Meals and equipment grants	Community Grants
<b>Control weakness/risk</b>	<b>Likelihood of control weakness</b>				
Untimely receipt of funds	L	H	H	H	H
Insecure receipt of funds	H	M	H	M	H

**Untimely receipt of funds:** Each of the Ministries administering public grant monies indicated that the flow of funds from the Ministry of Finance was less than timely, indicating that the CPV process with the Ministry of Finance was inefficient and untimely. It is noted, however that this process has been addressed since 30 June 2007 with the introduction of the Transition Budget.

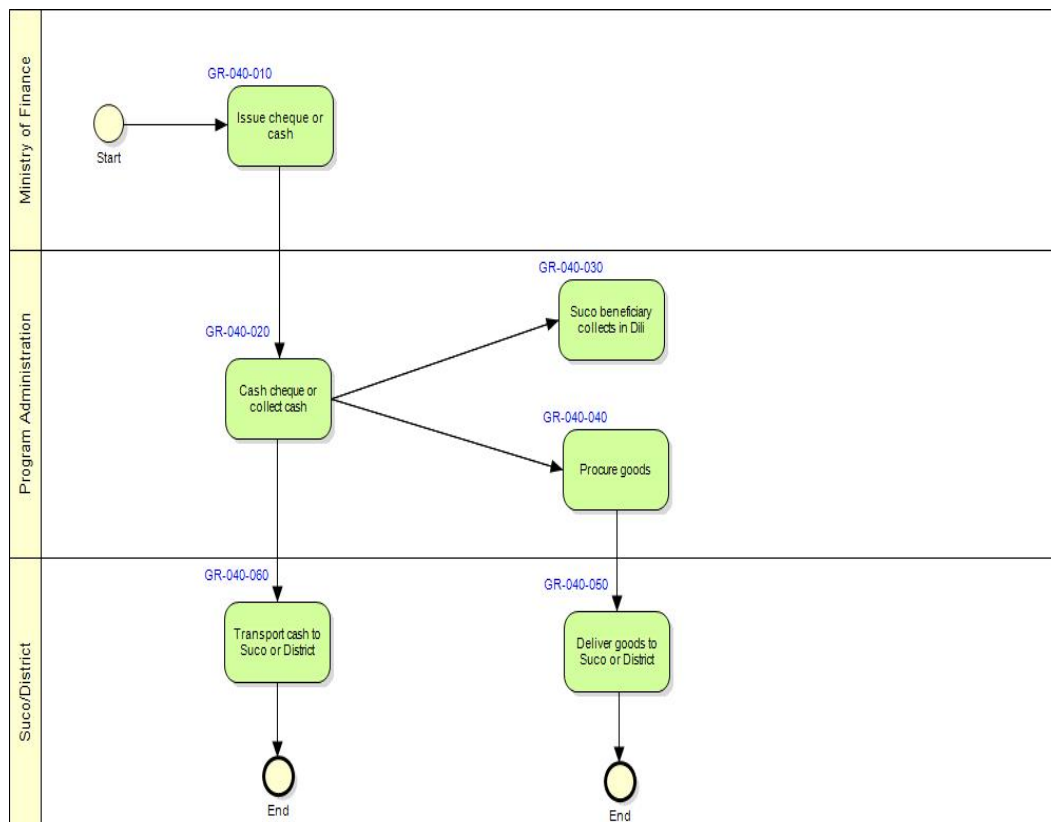
Reference should be made to the Review of the RDTL Procurement Process Report for risks and issues regarding the CPV processes within the Ministry of Finance.

**Insecure receipt of funds:** The timely processing of the CPV is particularly important with the Solidarity Fund, where funding may be required at short notice. Consequently, the Ministry of State Administration collects significant cash holdings from the Ministry of Finance and maintains these cash holdings on their premises to meet the needs of the community in crisis situation. The premises is not considered adequately secure for such significant cash holdings.

Similarly, the Community Grant funds administered by the MoAFF is required to transport significant sums of money into the remote and rural regions of Timor with some assistance from the UN in terms of security arrangements. Security arrangements with the UN will not be a sustainable solution for the future.

### 3.7 MAKE PAYMENT TO COMMUNITY BENEFICIARIES OR SUPPLIERS

Cash is a highly liquid commodity and cash handling practices are insecure and risky particularly in the environment of a developing country such as Timor-Leste.



A summary of risks and issues identified within this sub process is as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	School Meals and equipment grants	Community Grants
<b>Control weakness/risk</b>	<b>Likelihood of control weakness</b>				
Risk of invalid payments	H	H	H	H	H

**Risk of invalid payments:** The risk that invalid or excessive payments are made to community beneficiaries or suppliers of goods whether it be by way of error or fraudulent misappropriation of funds is considered to be very high for each grant program. The main reasons identified for this being:

- There are significant sums of money being held either at the respective Ministry offices in Dili and/or physically transported from the Ministries into the community by administration staff.

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- Security surrounding the physical location of cash storage is not optimal. Ministry offices in Dili are in some cases effectively operating as small community banks, yet the physical location of the safe holding the cash is not built for the purpose of secure banking activities, and staff have limited financial and accounting training.
- When funds are transported into the community, unsafe practices have historically been adopted.

*Example: Cash delivery*

*Transport of cash funds to a district for the purpose of one of the grant programs necessitated the Director of Finance and Administration risking his own safety to personally deliver cash disguised within an ordinary object of his vehicle in order not to attract attention.*

- Once Ministry staff arrive at the district, there may be further issues such as:
  - community representatives from the Suco may not be present to receive the cash proceeds upon arrival of the Ministry staff.

*Example:*

*As a necessary security measure, the Ministry of Agriculture, for example, will not always specify the exact day that they will arrive at the district to deliver cash funding, instead providing indicative timing.*

- or the identity of the community representative may be difficult to confirm before handing over cash.
- Once received by the community representative, there is no guarantee that representatives will pass the full shipment of cash over to the community.

*Example: Lautem - Tutuala*

*The Community Development Fund established by the Ministry of Agriculture have had reports in the Lautem – Tutuala region that the village chief did not distribute cash funds to the wider village once received.*

- Technology is in place in some districts for electronic transfers of funds to be made to bank branches in four districts, however the capacity of staff and IT systems is not always reliable to ensure the accuracy of the transactions.

### 3.8 MONITOR PROGRESS AND PAYMENTS

Where funds are applied by the community contrary to the activities outlined in the original proposal, it is unlikely that funds will contribute toward the achievement of the strategic objectives of the Ministry and the wider Government. The objective of monitoring the progress of programs and payments made throughout the duration of the program is to promptly identify any leakage of any funds toward inefficient and ineffective areas in the community as well as to help review the extent to which adequate resources are being allocated to the administration of the fund activity.

There are two fundamental elements of monitoring grant programs:

- i) performance monitoring, to monitor the physical progress of program activities, and
- ii) financial monitoring, to monitor the costs and funding outlays.

There appears to be limited formal monitoring procedures conducted prior to the acquittal process.

A summary of risks and issues identified within this sub process is as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	School Meals and equipment	Community Grants
<b>Control weakness/risk</b>	<b>Likelihood of control weakness</b>				
Lack of effective monitoring strategy	H	H	H	H	H
Decentralised monitoring	M	M	L	H	H
Poor record-keeping	H	L	M	H	L
Budget excess	H	L	M	H	L
Costs of maintenance	L	L	M	H	L
Standards not set	H	M	M	H	H

**Lack of effective monitoring strategy:** Despite evidence of some level of monitoring activity within each grant program, there was no evidence that any formal monitoring strategies had been adequately developed by any of the public grant program administrators and certainly no risk-based strategy linked to any fraud control planning.

The extent and timing of monitoring activities can be very challenging in an environment such as Timor-Leste where there are a large number of relatively low-value grants provided to the community by each Ministry. Community recipients and responsible officers generally have limited resources to effectively monitor and report activities.

However, in such an environment the importance of an effective monitoring strategy is ever more increased.

**Decentralised monitoring practices:** Where monitoring procedures have been applied by Ministries, they have been applied in a decentralised manner. Decentralising the responsibility to monitor the progress of grant programs serves is good practice; however care needs to be taken that:

- sufficient resources are consistently available
- segregation of duties is not compromised
- monitoring standards are consistent between regional areas
- independence of the decentralised monitoring staff is not eroded over time
- a level of centralised monitoring is also maintained

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*Example: Community Development Fund – Monitoring Practices*

*There is a lack of Ministry staff in all districts available to monitor the agriculture programs. The Ministry of Agriculture have reported that there are only 5 staff to cover all the villages in one district.*

*Reports regarding physical progress of agriculture activities and breakdown of expenditures appeared to be inconsistent in format and content between regions.*

*Example: Decentralisation – Community Development Fund*

*Decentralised monitoring procedures have enabled specific cases to be identified by the Ministry of Agriculture where grant funds were not spent in accordance with the agreed objectives of the fund. Including:*

*Dili – Bidau Lecidere and Dili – Caicoli where recipients did not use funding for the stipulated purposes. In one instance, funds were provided to a village and instead of being used for the acquisition of animals, used to establish a restaurant.*

*Monitoring of the Community Development Fund administered by the Ministry of Agriculture is largely conducted by the Ministry staff within each district and facilitators nominated by each Suco.*

*There is a risk here however. There is a lack of segregation of duties where locally based personnel have (at times):*

- custody of the cash funding*
- assist with recording the distribution of cash funds, and*
- responsibility for monitoring and reporting to the Ministry*

*This environment provides a level of power and authority to the locally based staff. They are entrusted by the Ministry to administer the rural programs in an honest manner whilst they continue to live as part of the community that will benefit from the appropriation of funds.*

*In order to ensure the independence and loyalty of the Ministry staff based in local communities, staff rotation and/or a level of centralised monitoring activity may be required.*

*Example: Decentralisation – School feeding program*

*Similarly, the School feeding program relies on the District Education Officers to, at times, procure and monitor the distribution of goods to recipient schools without any centralised monitoring strategy.*

A level of centralised monitoring will be important to a largely decentralised monitoring strategy, particularly for purposes of lodgement of any complaints or reporting of fraudulent activities.

The complaints process relies partly on verbal reports to district based staff and partly on written letters to the Ministry office. Many community beneficiaries, however, do not read or write and may not always be able to address their concerns directly with district staff.

**Poor-record keeping:** There are vast differences in the standards of record-keeping between Ministries. Poor record keeping practices significantly expose the Government to heightened potential for error and fraud.

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*Example: Good Practice – Solidarity Fund*

*The Solidarity Fund had detailed Excel based accounting records for each of the numerous programs within the Solidarity Fund as well as cash balance reconciliations to the daily cash balance held within the safe. Despite the lack of finance and accounting training of the two personnel who administer the cash distributions, the accounting records were considered to be well managed.*

*Example: Poor Practice – School Feeding Program*

*Accounting records kept for the School Feeding Program were considered to be poor.*

*Key documentation such as food and utensil delivery dockets and receipts for cash are kept loose leaf in a manila folder. Documents are not adequately filed and no filing system appears to exist.*

*Upon request, no summary could be readily provided to account for fund monies spent to date of the 2006/07 budget allocation. Loose leaf CPV documents were tallied up manually in order to derive an estimate of the possible spend.*

*Reconciliations of cash holdings within the safe are apparently checked and balanced to the records only at the date a transaction occurs. Should cash be stolen from the safe in the interim period, it is likely that it would remain undetected until the next funding transaction occurred.*

**Budget excess:** Although there is significant carry over amounts from the 2006/07 budget for each of these public grant funds in aggregate, the risk that individual areas within the public grant fund are operating over budget is still considered a possibility, particularly into the future where there is an apparent lack of a disciplined monitoring procedure. There was no evidence presented by the Ministry of Education that actual expenditure with suppliers and schools for particular goods was being monitored against any detailed budget, for example.

**Costs of maintenance:** The main costs associated with administering large grant programs within a Ministry should be captured, recorded and monitored. The Ministry of Agriculture was the only Ministry to demonstrate that such costs were being accounted for in any detail.

**Standards not set:** Standards of frequency, consistency, quality and format of monitoring throughout the duration of individual programs (prior to the acquittal process) have largely not been set.

### 3.9 ACQUIT FUNDS

Reliable, timely and adequately documented procedures are required to ensure financial accountability at the conclusion of the program or at stages of key milestones during the program.

Many of the Public Grant funds across the relevant Ministries did not have adequate or well-documented arrangements to ensure effective financial accountability further exposing each fund to the potential for fraudulent practices to go undetected.

A summary of risks and issues identified within this sub process is as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	and equipment grants	Community Grants
Control weakness/risk	Likelihood of control weakness				
Funds applied to unauthorised activities	H	M	M	H	H

**Funds applied to unauthorised activities:** There were no best practice acquittal forms or acquittal procedures demonstrated by any of the Ministries. Ministries also have a backlog of acquittal reports exposing each of the funds to potentially having had expenditures applied to unapproved activities. This further emphasises the need for a co-ordinated monitoring strategy to be implemented throughout the duration of these public funded programs.

*Example: Acquittal reports – School Feeding and equipment Program*

*No acquittal reports were evidenced. The only documents available were unfiled loose leaf receipts from the districts.*

*An example of a receipt for payment of a sugar delivery was viewed and noted as having no evidence or verification from any party as to the physical quantity of sugar actually delivered or paid for. This exposes the government and the local schools to potentially receiving food quantities less than ordered.*

*Example: Acquittal reports - LDP*

*District and sub-district assemblies are required to prepare monthly expenditure reports to the District Administration Treasury, which will be forwarded to the Ministry of State Administration. However, there have been instances of untimely reporting.*

*There exists a backlog of acquittal reports for recurrent expenditures due reportedly to other pressing priorities and difficulties in sourcing invoices from the community.*

*Example: Acquittal reports – Ministry of Agriculture*

*When requested to view acquittal reports, although individual files were maintained, financial information from the Suco was extremely light with little detail and a few items of photographic evidence making it difficult at times for the Ministry to evaluate compliance with the terms and conditions of the 40% and 60% funding activities.*

*Despite the Ministry of Agriculture investing significant time and energy into the development of a framework and proforma documentation for the execution of community grant programs in the rural area, there is no guidance provided to the community with regard to the expected content of acquittal reports. Key performance indicators or key milestones outlined within the original proposal may not be addressed.*

*Key performance indicators could be financial or non-financial. For example, targets such as the acquisition of a specified number of cattle.*

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Financial and non-financial performance information can be assisted by common design of acquittal forms or reports within or across Ministries. In the absence of any proforma acquittal reports, beneficiaries are less able to demonstrate that program objectives (financial and non-financial) have been achieved. Acquittal reports should be designed in such a way that reference is clearly made to the key performance indicators (financial and non-financial) that should be established during the design of the program objectives and framework.

When asked, only the Ministry of Agriculture was able to articulate specific cases known to them of potential or alleged misappropriation of funds that had or were in the process of being investigated. It is observed that the Ministry of Agriculture has a framework which monitors progress of activities to which funding is applied throughout the year and limits funding by way of staged distributions.

### 3.10 EVALUATE PROGRAM FOR THE FUTURE

The purpose of an evaluation of the overall Ministry program is to assist program administrators to determine:

- the continued relevance of the program to the community
- the effectiveness of achieving the Ministry's stated strategic objectives
- the identification of future improvements that could be made in achieving these objectives
- whether the level of resourcing to administer the program is adequate
- whether fraudulent practices are being adequately identified
- the need to establish new programs or initiatives

A summary of risks and issues identified within this sub process is as follows:

	Fraud Risk	Local Development Program	Solidarity Fund	and equipment grants	Community Grants
<b>Control weakness/risk</b>	<b>Likelihood of control weakness</b>				
Continued program weaknesses	H	H	H	H	M

**Continued program weaknesses:** Without an effective evaluation process, any control weaknesses in the grant funding processes will continue into the future. Control weaknesses most sensitive to the risk of fraud that continue unaddressed may foster a culture of funding abuse. Control weaknesses less sensitive to the development of fraudulent activities will instead promote continuing inefficiencies and ineffectiveness in future programs.







Without stating the program objectives in a manner that is clearly measurable at the outset, it is difficult to have a basis upon which an objective and effective evaluation exercise can be conducted. This is largely the case with each of the Public Funds reviewed.

It should be noted, however that the Ministry of Agriculture has commenced the process of considering the strategic direction and operation of its community grants within its Community Development Fund Report 2007. Issues are acknowledged within the report with proposed solutions stated.







Reviews and evaluations, if conducted by Ministries could be used to benchmark similar or common components of the public grant processes. By leveraging the knowledge shared between Ministries, this could benefit those Ministries in need of improving their processes in a cost effective manner.

## 4.0 RECOMMENDED ACTIONS













A summary of recommended actions to address the risks and issues identified in this report is presented in the table below:

Risk/Issue	Systemic Risk	Fraud Risk	Complexity to address	Recommendation
Management of carry over funds				It is recommended that the Ministry of Finance formally establish a permanent guideline or directive as to how the Ministry of Finance intends to practically apply the law regarding the timeline for access to carry over funds in future periods.
Security of Solidarity Fund cash transactions				<p>It is recommended that either:</p> <p>a) the office of the Ministry of Labour &amp; Solidarity have the physical security of its premises upgraded to that of a financial institution; or</p> <p>b) not be used as a banking institution, but instead take on the role of authorising distributions to be made to the community from a major banking institution (eg BNU). Financial delegation of authority to withdraw cash from the Government bank account would need to be reviewed, however recipients would then collect cash distributions directly from the secure bank facilities in Dili, rather than the Ministry office.</p> <p>In the meantime, a contingency plan should be developed for additional resources and security measures to be allocated and actioned at the Ministry of Labour &amp; Solidarity in the event of another crisis.</p>










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Risk/Issue	Systemic Risk	Fraud Risk	Complexity to address	Recommendation
Duplication of funding sources between Ministries				<p>i) A forum should be established to regularly share information between Ministries to oversee the purpose and objectives of public funding programs within each Ministry in order to ensure there is no duplication, nor any conflict, of funding between Ministries. This could be a physical forum of meetings specifically convened for this purpose throughout the year, or alternatively a shared database or register of such programs between Ministries.</p> <p>ii) as each application for grant money is made to a Ministry from the community, the governing body responsible for evaluating the application should document reasons for its decisions to either approve or deny each application and expressly state as to whether there is any duplication of purpose of funding with funding sources of other Ministries.</p>
Proforma application forms for grant funds				Proforma templates for proposals or grant application forms made by the community should be provided by each Ministry wherever applications for funds are initiated by the community. The proforma document should at the very least, outline the minimum criteria and information requirements of the Ministry in order for the relevant governing committee to make complete, consistent and objective evaluations of all applications.







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Risk/Issue	Systemic Risk	Fraud Risk	Complexity to address	Recommendation
Ministry of Labour & Solidarity: Validity check of beneficiaries				Verification of military personnel identification with the Ministry of Defence made at the commencement of the application period for payments from the Solidarity Fund should be rechecked periodically throughout the year to ensure such individuals have not deceased.
Quality of accounting records				A summary of accounting record should be maintained by all Ministries administering Public Funds (such as the example of the Ministry of Labour & Solidarity). The summary should be updated at least monthly and would detail budgeted expenditure by program, committed expenditure, funds released by the Ministry of Finance and residual balances of funds to be released and available to the community. Where relevant, this summary should balance any cash holdings to those maintained within any safe kept on premises at the relevant Ministerial office.
Quality of record keeping				Ministries should ensure that an effective filing system is established to ensure an adequate audit trail is maintained. In particular, the Ministry of Education and Culture could benefit from an efficient filing system.
Daily cash reconciliations				Where public fund money is kept by a Ministry on-premises in a safe, daily cash reconciliations to accounting records should be made. This would ensure any stolen cash from the safe would be detected in a timely manner. Cash reconciliations should be checked and authorised by a second officer.







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Risk/Issue	Systemic Risk	Fraud Risk	Complexity to address	Recommendation
Lack of resources and training				There exist a lack of resources and training across many of the public grant programs. Ministries should ensure that budget submissions to the Ministry of Finance adequately budget for administration costs, such as salaries and training costs for an adequate number of resources and capacity of resources to help execute and administer their programs.
Administration and training Manuals				Administration of grant programs should be documented in detail, including job descriptions, roles and responsibilities of the various area of each Ministry in administering public grant funds. This will be of assistance when there are staff changes. Similarly, training manuals should also be documented.
Transport of cash to districts				<p>To address the security risk to administrative staff and fraud risk in transporting cash funds into the districts, it is recommended that:</p> <p>i) the government encourage and support the continued establishment of bank branches in as many districts as possible in the future; and</p> <p>ii) in the meantime, review the level of security being provided to administration staff in the transport of cash. Budget submissions to the Ministry of Finance may need to take security costs into account.</p>










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Risk/Issue	Systemic Risk	Fraud Risk	Complexity to address	Recommendation
Monitoring of grant programs				Decentralised monitoring of grant programs is encouraged where grants are high volume and low dollar value. However, it is recommended (for example, the Community Development Program) that where a decentralised monitoring program is in place, that: i) any locally based staff members responsible for a monitoring role be rotated between districts in order to preserve independence; or ii) alternatively, a central monitoring role be administered from Dili in addition to the decentralised functions to independently check on areas of highest risk (eg. areas where misappropriations have occurred in past years, areas with greatest grant funds, areas with new district staff)
Proforma monitoring reports and acquittal reports				All Ministries are encouraged to establish and provide to communities, proforma monitoring reports and acquittal reports. Assisting communities with the format of these documents would assist each district or Suco in articulating their business case for future funding and likewise assist each Ministry in an objective and efficient evaluation process as to whether the funds have been used effectively in the community.







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Risk/Issue	Systemic Risk	Fraud Risk	Complexity to address	Recommendation
Strategic monitoring programs				<p>It is recommended, that strategic monitoring programs be formally established and documented by each Ministry administering public grant funds, as well as the functions of IGE and PNTL.</p> <p>As with the Ministry of Agriculture, that monitoring of public grant funding should be conducted progressively throughout the year. In particular, the Ministry of Education and Culture could consider the introduction of monthly or quarterly reports from District Education Officers (and approved by Principals) regarding the delivery of food and equipment to schools.</p> <p>Strategic monitoring programs may include an element of both decentralised and centralised monitoring roles. Centralised monitoring functions would be risk-based and effectively oversight the decentralised monitoring functions.</p>
Fraud policy				<p>Processes regarding the communication of fraud or misappropriation should be clearly established and communicated to all stakeholders, including administration staff and the community. Without a channel to report fraudulent practices by all stakeholders, issues may never be reported or investigated.</p>

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Risk/Issue	Systemic Risk	Fraud Risk	Complexity to address	Recommendation
Adequacy of Delivery Records				<p>Wherever a Ministry has goods delivered to the community, the representative authorising or providing payment to the supplier should ensure that exact quantities of product delivered are noted on receipts and checked for accuracy, for example:</p> <p>i) Ministry of Education and Culture with regard to district deliveries of food and equipment to schools. Payment should not be handed over unless receipts specify the accurate quantity of goods which should agree with the original order made. Receipts including the delivery quantity should be signed by both the district education officer and the supplier; and</p> <p>ii) Example of the rice shipment, where no evident of shipping documentation was attached to any of the payment authorisation documentation.</p>
Legislative Framework of IGE				It is recommended that an appropriate legislative framework (eg Organic Law) be established for the operations of IGE to ensure activities are governed and objectives are clearly defined.
Exposure to cost overruns: IGE				Agreements between IGE and relevant construction contractors should be reviewed by professional legal advisors. In the meantime, it should be ensured that future contracts clearly stipulate, where relevant, that any cost overruns are to be met by the contractor rather than the government.

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Risk/Issue	Systemic Risk	Fraud Risk	Complexity to address	Recommendation
Comprehensive reporting: IGE				Comprehensive reports on a monthly basis for each contract detailing money received, yet to be received, stage of completion of contracts and costs to date should be monitored.
National Police of Timor-Leste procurement activities				It is recommended that the Ministry of Finance comprehensively consider any proposal put forward by the Cabinet of Inspection regarding the co-ordination of organisations in the community to assist with monitoring of anti-corruption activities. Should a forum for co-ordinated anti-corruption monitoring activities be convened, it is recommended that the Ministry of Finance be represented at that forum and by individuals independent of any procurement function.

## 5.0 SUMMARY FINDINGS OF OTHER KEY AREAS

### 5.1 CONTINGENCY RESERVE

The use of funds within the Contingency Reserve has significantly increased during Fiscal Year 2006/07 compared with the financial activity of 2005/06. Activity within the reserve is summarised as follows:

	2005/06 \$USD	2006/07 \$USD
Actual Expenditure	543,534	2,620,165

Key observations relating to payments from the Contingency Reserve during the past two years were as follows:

Reference Number	Vendor Record	Activity Description	\$USD	Note
P73785	Ensul	Other Services	149,600.00	A
P75644	Ensul	Other Supplies	147,200.00	A
P76689	Ensul	Construcao do Centro de Aquart	32,800.00	A
C30725	No Vendor	Para Elecoes Presidencial	49,300.00	B
P71654	No Vendor	Contribution GRN Police	10,680.00	C
P71893	No Vendor	Other Services	101,129.48	D
P73156	PT LEN INDUSTRI ( PERSERO )	Other Services	196,740.00	E
P74764	PT LEN INDUSTRI ( PERSERO )	Other Services	196,740.00	E
P74191	TALI-META, UNIPESSOAL Lda.	Other misc. services	135,464.40	F
P74376A	TIMOR GLOBAL (TL) Pte.Ltd.	Aquisicao de arroz	500,000.00	G
P76183	TIMOR GLOBAL (TL) Pte.Ltd.	Despesas operacionais	35,200.00	G
P73777	Other	Services	12,500.00	H
C20844	Other	Misc Services	220,500.00	I
P64267	Other	Services	45,000.00	I

- A. These payments were part of a series of payments to construction contractor, Ensul for the construction of barracks for GNR. The contract was negotiated in March 2007. Utilisation of the Contingency Reserve was approved by the Prime Minister.
- B. Cost of drivers and polling staff for 2007 elections. Invoices were authorised by the Prime Minister.
- C. Being payment to Sunshine Petrol Group for 12,000 litres of diesel for the GNR. Delivery docket attached, however no approval from Prime Minister evident.
- D. Provision of food to GNR by Leader – Lisun. Invoicing was approved by the Prime Minister.
- E. These payments were for additional costs of a contract, indicative of poor contract management. An increase in costs of more than 30% of the original contract price were paid to PT Len Industri for the supply and installation of TV and radio transmitter stations. A contract variation had to be negotiated for additional works of \$393,480 increasing the original cost of US\$910,000 to US\$1,303,480. Invoicing was authorised by the Prime Minister.

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- F. Provision of polling kits and stationery immediately prior to 2007 elections. Invoicing was authorised by the Prime Minister.
- G. A payment of \$500,000 was charged to the Contingency Reserve in excess of the amount of Solidarity Funds available for a major acquisition of rice in March 2007. A contract to the value of \$960,000 was agreed between the Ministry of Labour and Community Reinsertion, Ministry of Finance and Timor Global (TL) Pte Ltd for 2,000 Metric tons of rice during the rice shortage in 2007.
- Although the request to use the Contingency Reserve was authorised by the Prime Minister, there was no shipping documentation attached to the documentation presented for payment.
- One very poor photocopy of a cargo manifest was found attached to a separate payment voucher made out to the stevedore company handling the same rice acquisition for \$35,200. However this shipping mandate was for a different quantity of rice (3,000 Metric ton) and annotated as “donated by P. R. China” inconsistent with the Timor Global contract. Further, the costs charged to the Timor Government for the transport and warehousing of the rice shipment were charged for an amount of 3,000 Metric tons rather than the 2,000 Metric ton in the contract.
- H. Each presidential candidate in 2007 received a \$12,500 payment to support their campaign. Original request was for \$7,500 per candidate. Payments were authorised for \$12,500 each.
- I. Invoices could not be presented by the Ministry of Finance. Record keeping system does not appear to support timely retrieval of records.

#### **National Police of Timor-Leste (PNTL)**

Observations from our enquiries were as follows:

- The Cabinet of Inspection in association with the newly centralised finance unit within the Secretary State of Securities has recently taken on new responsibilities for monitoring financial transactions of the PNTL.
- In a relatively short period of time, the Cabinet of Inspection has noted and is in the process of investigating numerous transactions that exhibit inconsistencies indicative of misrepresentation and potentially fraud. Examples of the nature of some of these transactions being:
  - suspected bias or inequity in supplier contracts awarded;
  - continuation of expired contracts beyond contract termination dates;
  - significantly inflated prices for supplies;
  - inconsistencies in invoicing. For example, services for repairs and maintenance being invoiced too frequently, vehicles serviced on the same day in more than one location, different types of fuel purchases for the same vehicles, etc.
- It was also represented that there have been difficulties in effectively verifying the inventory of assets such as police vehicles or computer equipment.
- It would appear that the preliminary investigative procedures being conducted by the Cabinet of Inspection are operating effectively.

- To ensure the success of the continued investigation of these cases and follow through enforcement of penalties, it is the view of the Cabinet of Inspection that the framework by which such indicative fraudulent practices should be reviewed, pursued and prosecuted needs to be a co-ordinated effort with other organisations in the community guided and supported by strong leadership of the government.

## **APPENDIX A: ABRIDGED TERMS OF REFERENCE**

### **A. BACKGROUND**

The 4<sup>th</sup> Constitutional Government of Timor-Leste was inaugurated on 14<sup>th</sup> August 2007. Since that time, the Government has been putting in place its structures, systems and processes to establish a working Government for the next term. Part of this effort has been learning of the structures, processes and operations of the previous Government. This process has been made more difficult by the lack of a comprehensive handover of matters by the previous Government.

The Government is required within a month of inauguration to present to Parliament its plan for its term of office. Within 90 days of the inauguration, it is required to have passed Organic Laws that govern the operations of each of the organs of State.

The Government will, as soon as possible put to the Parliament a "Transitional Budget" – a maintenance Budget to allow the functioning of Government prior to the formation, approval and promulgation of a new budget for the 2008 calendar year. (Note: since 1 July the government has been operating on a "supply" basis). The Government will immediately commence processes to develop the 2008 calendar year Budget with a view to having this placed before Parliament by mid November 2007

### **B. OBJECTIVES**

The government wishes to undertake a number of audits to assist in these processes and in the ongoing development of open, transparent and accountable Government. These audits should be designed to provide the following information to Government based on the past 5 years :

- The systems, processes and practices that govern certain key areas and activities of Government;
- The adequacy of the number and capacity of currently assigned human resources including both international advisors and national staff;
- The controls required to ensure integrity of these programs and the degree to which these already exist and are effective;
- The steps that are required to fix anomalies and deficiencies in the controls, systems and processes, and
- Identification of areas in which the operation of controls would suggest that the government has a significant exposure (potential or current) to inefficiencies, fraud and corruption.

In addition to the activities specifically addressed in this TOR, the Government is proposing to commission a separate audit of the following major functions:

- The National Customs Service.

The Government will very shortly commence its annual financial Audit of the financial accounts. This audit is outsourced to an international chartered accounting firm. The scope of this audit is attached in attachment 1. (Note: the attached TOR covers FY 2004/2005, however this has subsequently been amended to cover FY 2005/2006 and 2006/2007). In responding to this TOR, Auditing Companies (herinafter called Consultants) should consider the extent of overlap between the two activities and the opportunities for sharing information to enhance both programs.

### **C. SCOPE OF AUDIT SERVICES**

To meet the foregoing objectives, the audit services should address areas of high risk.

The Government's current assessment of these areas suggests:

1. Significant discretionary grants programs.  
These are:
  - a. The Solidarity Fund (Ministry of Labor and Solidarity - \$5m);
  - b. The Community Grants Funds (small infrastructure grants of about \$4.8m under Ministry of Agriculture Forestry and Fishing, social activity grants of around \$1m under the Prime Minister's Office);
  - c. Local Development program (Ministry of State Administration – for Grants to District Administrators - \$342,000);
  - d. School meals and school Equipment grants (Ministry of Education and Culture, \$2.2million);
  - e. Veterans (Ministry of Labour and Solidarity \$1.0m, Ministry of Finance (pensions) \$2.0m);
  - f. Contingency Reserve (Ministry of Finance - \$3.0 m);
  - g. Compensation for damage and loss in the Crisis (Ministry of Labor and Solidarity \$9m).
2. Autonomous and revenue collection agencies:
  - a. Customs Service \*
  - b. Procurement service
  - c. TLRS

\* 2a is currently proposed for separate audit and therefore should not be considered as part of this audit program.

## **APPENDIX B: STATEMENT OF RESPONSIBILITY**

In performing this service, Deloitte applied APS8, the Professional Statement on Management Consulting Services issued by the Australian Accounting Bodies.

Where Deloitte has provided advice or recommendations to the Government of the Democratic Republic of Timor-Leste, we are not responsible for whether, or the manner in which suggested improvements, recommendations, or opportunities are implemented. The Government of the Democratic Republic of Timor-Leste, or their nominees, will need to consider carefully the full implications of each of these suggested improvements, recommendations, or opportunities, including any adverse effects and any financing requirements, and make such decisions, as they consider appropriate.

The work performed did not constitute an assurance engagement in accordance with Australian Auditing Standards.

The matters detailed in our report are only those which came to our attention during the course of performing our procedures and did not necessarily constitute a comprehensive statement of all the risks or issues that exist or actions that might be taken. Accordingly, management should not rely on our report to identify all risks and issues that may exist in the systems and procedures discussed. The report should be read in the context of our terms of reference. Had we performed additional procedures or had we performed an assurance engagement in accordance with Australian Auditing Standards, other matters might have come to our attention that would have been reported to you.

This report and all deliverables have been prepared solely for the use of the Government of the Democratic Republic of Timor-Leste, and should not be quoted in whole or in part without our prior written consent. Our work or the report may not be sufficient or appropriate for any one else's purposes. We have no duty of care to anyone, other than the Government of the Democratic Republic of Timor-Leste for the work we have performed or for the report or anything in it and we are not responsible to any third party as the report has not been prepared, and is not intended, for any other purpose.

The report may not address or reflect matters in which any one other than the Government of the Democratic Republic of Timor-Leste may be interested or which may be material to you. Events may have occurred since we prepared the Report which may impact on the information contained in the report.

We have agreed that this Report may also be translated into Tetum and Portuguese (the Translated Reports). We have not reviewed the Translated Reports and make no representations or warranties that the Translated Reports are a true, complete and accurate translation of the Report. We are not responsible to you or anyone else for any errors or omissions in the Translated Reports or if you or anyone else chooses to act, or refrains from acting, on the basis of the Translated Reports.

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