CHAPTER 8

Securing a New Ordering of Power in Timor-Leste: The Role of Sub-national Spending

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A crucial aspect of Timor-Leste's economic performance and political stability in the aftermath of the 2006 crisis has been the way the government has managed a five-fold increase in public spending, and an even more rapid increase in capital spending. While the country's experience has been widely acknowledged as an exemplar of 'buying the peace', less well documented has been the range of unorthodox arrangements adopted by the government to manage this fiscal expansion and to re-order the local political landscape. Sub-national spending was pivotal, despite amounting to only around 3 per cent of the budget. Recent research undertaken by the World Bank,² including a joint study with the Government of Timor-Leste of its sub-national development programs, provides empirically grounded insights into how public spending can be used to dynamically trade-off and balance competing technical, social and political priorities in the immediate aftermath of conflict. This chapter's assessment of

1 The authors are staff of the World Bank who worked on the study discussed in this chapter, *Sub-national Spending in Timor-Leste: Lessons from Experience* (World Bank, Justice for the Poor, 2014). documents.worldbank.org/curated/en/2014/11/20426607/timor-leste-sub-national-spending-lessons-experience. However, the views expressed in this chapter are not to be attributed to the World Bank, but are the authors' views, based on several years of engagement in Timor-Leste in different capacities. The authors are grateful for advice from Sue Ingram, Bjorn Dressel, Anthony Goldstone and Edio Guterres, and acknowledge comments by participants at seminars at which these findings have been discussed in Canberra (18/4/2013 and 28/11/2013), and Washington DC (25/11/2013 and 23/4/2014).

2 This includes studies of large infrastructure contracts; a political economy analysis of sub-national spending that draws from new qualitative research as well as synthesising existing literature; and a broader contemporary political economy analysis of the country, drawing from an analysis of its history.

public spending provides a lens through which to understand the crafting of political settlements in contexts where securing stability is paramount. The nature of the emerging settlement, in turn, shapes spending outcomes.

Introduction

In the initial post-independence period after 2002, Timor-Leste was heavily aid-dependent and its leaders had few resources through which to pursue policy aims. Over the subsequent years, an exclusivist political dynamic had developed, regional tensions began to run high, and unrealistic expectations fuelled a growing sense of grievance that culminated in the eruption of violence in 2006.³ The fiscal expansion since 2007 was financed through sharply rising petroleum revenues and utilised government systems to plan and budget, spend and account for results. Annual capital and development spending peaked around US\$555 million in 2011 (World Bank 2014: 1). This contrasts with the annual average of US\$55 million in the years prior to 2007, which was mostly donor-funded and managed under donor procedures.

This chapter examines one aspect of this fiscal expansion, namely sub-national capital spending. We view the arrangements for sub-national spending in two ways. In the first part of this chapter, we summarise the findings of a World Bank/Banco Mundial and *Ministério das Finanças* (Government of Timor-Leste Ministry of Finance) evaluation of how different sub-national spending programs performed in meeting immediate policy objectives: stimulating a domestic contractor sector, creating jobs, building infrastructure, avoiding a relapse of conflict in the near term. We then turn to reflect on how these mechanisms contributed to larger, although closely related, 'strategic' purposes, including the imperative to consolidate a new elite bargain by economically empowering previously disenfranchised social and political constituencies. This spending was more than buying the peace in the short term; it was also about a re-ordering of Timor-Leste's political economy that began with the advent of the Petroleum Fund in 2005, control of which has animated politics ever since (Rees 2013).

3 The 2006 crisis was sparked by a group of petitioning soldiers (called the 'petitioners'), predominantly from the country's western districts, who charged their army superiors, who were predominantly easterners drawn from the Resistance armed forces, with discrimination in the national army. The subsequent sacking of nearly 600 petitioners by the government led to widespread unrest and violence.

In \$ millions

Figure 8.1 Major infrastructure spending FY 2004 – FY 2013 (US\$ millions).

Source: World Bank 2014: 1.

Innovations in sub-national spending: the *Pakote Referendum* in brief

The *Pakote Referendum* (Referendum Package), named for the 10-year anniversary of the 1999 independence plebiscite, was announced by Prime Minister Gusmão in a supplementary budget speech in August 2009. In what had been dubbed ‘the Year of Infrastructure’, the government was struggling to disburse the budget allocation for infrastructure. In August, it reallocated US\$70 million of unspent funds to the *Pakote Referendum*. In doing so, it was responding to the demands of an evolving political economy, and the idea of delivering an ‘independence dividend’ to Timor-Leste’s citizenry. The *Pakote Referendum* handled only a modest share of national spending, but it represented a critical effort to address economic, social and political priorities in the aftermath of conflict. Its professed aims were to:

1. create a local entrepreneurial class by capitalising Timorese contractors
2. generate employment
3. deliver quality infrastructure.

These policy priorities were often in tension, and the relative emphasis given to each has shifted over time as the *Pakote Referendum* was refined through subsequent iterations of the *Programa Dezenvolvimentu Decentralizado* (PDD; District Development Program). Today they are known as ‘PDID projects’.⁴

As a spending modality, the *Pakote Referendum* was risky but innovative. By creating a group known as the *Associação Empresários Construção Civil e Obras Públicas* (AECCOP; Entrepreneurs’ Association for Construction and Public Works) at national and district levels, the prime minister embarked on a radical decentralisation of power and authority at direct odds with the logic and prescriptions of ‘good governance’. Rather than devolve power to lower level government authorities, the *Pakote Referendum* created market entities and empowered them to handle public expenditure. AECCOP’s leadership, closely affiliated with and trusted by senior members of the government, was given responsibility for identifying some 700 small- to medium-sized projects, allocating the funds, awarding projects to their members, and supervising all project implementation. Moreover, during its initial roll-out in 2009, the entire process was not governed by any formal regulations. This bold move was unsurprisingly greeted by a chorus of concerns from the political opposition, civil society and donors about its fiscal sustainability, governance and accountability arrangements. Some donors threatened to pull out of a US\$34 million World Bank public financial management reform program, but had yet to grasp that the surge in the country’s oil wealth had radically diminished their influence.

The *Pakote Referendum* and its successor programs were part of a suite of measures introduced to respond to the political dynamics following the 2006 crisis. It has been widely acknowledged that Timor-Leste was fortunate in having established a sound architecture for fiscal management in the form of the Petroleum Fund and a reasonably well-defined public financial management system before the surge in oil revenues. Yet these arrangements also placed extraordinary pressure on the minority coalition government—the *Aliança Maioria de Parlamentar* (AMP; Alliance of the Parliamentary Majority)⁵—when it assumed office in August 2007. Unusually for a post-conflict scenario, there were no off-budget rents for government to distribute in pursuit of near-term political and social stability.

4 *Planeamento de Dezenvolvimentu Integradu Distritál* (Decree Law for Integrated District Development Planning or PDID) came into effect in January 2012 and now governs a number of different sub-national spending programs.

5 FRETILIN, which had been in government since independence, found itself short of a majority in parliament and unable to secure a majority coalition. Three other parties – *Conselho Nacional de Reconstrução de Timor* (CNRT), *Partido Democrático* (PD) and *Associação Social-Democrata Timorense-Partido Social Democrata* (ASDT-PSD) – formed a majority coalition named the *Aliança da Maioria Parlamentar* (AMP); this was later joined by a further party, *Unidade Nacional Democrática da Resistência Timorense* (UNDERTIM). The durability of this coalition required considerable political and public spending compromises to maintain, many of which were seen in 2008.

Public spending through the existing, but in many respects untested, architecture provided the only means available to stabilise the country and shape the emerging elite bargain—by bringing political opponents and potential spoilers with the capacity to mobilise violence ‘into the tent’, reward party supporters and allies, and meet the demands for an ‘independence’ dividend from the broader populace.

Public spending and post-conflict transition—the larger story in Timor-Leste

The 2009 supplementary budget was the government’s fifth since August 2007; in rough terms, each of these budgets had doubled the outlays of the one before (Porter and Rab 2010). The government began entering into a wide range of agreements for large infrastructure projects (such as sea and air ports, power and transmission projects, and oil sector equity production arrangements), with the professed aim of increasing annual gross domestic product (GDP) growth beyond 8 per cent and diversifying the economy. To lift the rate of spending, the government opened many new spending lines; more spending powers were delegated to line ministries; and spending increased on goods and services, including subsidies on essential commodities. An expansive social protection scheme was introduced, including universal pensions for the elderly and people with disabilities, conditional cash transfers for school-going children in vulnerable households, support to veterans and survivor families, and ad hoc responses to internal displacement and natural disasters. The *Pakote Referendum* was part of this fiscal expansion.

Figure 8.2 PR/PDD and PDL budgets (US\$ millions).

Source: World Bank 2014: 4.

Seen through the lens of the post-conflict transitions literature, it could be argued that the government's spending was sending what have been termed 'credible signals of change' to the populace focused on three areas: security (of person and property, but also broader political stability and social order); justice (avoiding egregious exclusion in access to public wealth and economic opportunity); and jobs (a reasonable expectation of a dignified existence and the opportunity to accumulate wealth and assets) (World Bank 2011). The government was signalling that citizens would be protected from the global food and commodity price crisis that emerged in 2008, and they would derive immediate benefits from the surge in oil wealth. Key was the economic empowerment of previously disenfranchised social and political constituencies, including the veterans of the Resistance struggle and their families, disaffected members of the military, and those from western regions of the country who were perceived to be excluded.

Principal among these groups were veterans, particularly those who lived in rural areas, and were not part of the national political or economic discussion. Whether under the Portuguese colonial administration or the Indonesian occupation, the elite bargain was created and held together by a mix of force and incentive. Until 2002, participants in the bargain were few in number. There were few Timorese contractors in the country except for a handful that had collaborated with the Indonesian military, and none at the time with the capacity to execute large-scale contracts. In the post-independence democratic context, the accommodation of the large veterans constituency posed a critical challenge. Until the Petroleum Fund and the surge in oil wealth thereafter, government did not have the means to deal with this fractious and largely impoverished group. The *Pakote Referendum*, among other mechanisms, aimed to economically empower veterans by distributing public contracts to them, thus providing them with a real stake in the new political and economic order that was being constructed and ongoing incentives to participate and co-operate.

The tactical and strategic purposes served by sub-national spending speak to an emerging consensus about what typically occurs in successful transitions out of conflict. Thematically, the World Bank's 2011 survey of experience and scholarship contends that successful regimes need to send 'credible signals' of a break from the past. Longer term legitimacy derives from 'institutional transformation' whereby incentives are created to deliver services inclusively, rather than simply distributing resources to particular actors through forms of patronage that can corrode trust and ultimately exhaust available resources (World Bank 2011). This lens on post-conflict transitions provides one way to frame the challenges faced by the government soon after it came into office. The government had a fragile electoral coalition to consolidate—there was considerable political fluidity, high expectations, and a lively public debate,

including through parliament. There was also a palpable threat of instability (Engel and Hanley 2007). Around 150,000 internally displaced people were still in camps close to Dili. While there had been a dramatic economic recovery—8 per cent GDP growth in 2008, after negative 6 per cent GDP growth in 2006—the private sector was stagnating, and private spending was contracting with the onset of the 2008 fuel and commodity crisis. An additional 16,000 youth each year were looking for work and a reasonable expectation about the future. Anecdotal evidence was circulating that poverty and inequality were increasing.⁶ There was a sense of injustice among key political constituencies and perceptions of an ‘east–west’ regional divide. While government had announced a path from ‘stabilisation’ to ‘recovery’, its first task was to maintain social order and stability.

In the face of these multiple pressures, the government acted pragmatically. It was not convinced that existing mechanisms to spend public wealth would be able to move quickly enough or enable it to effectively reach key constituencies. This was especially the case with sub-national spending. A mechanism already existed in the form of the donor-supported *Programa Dezenvolvimentu Lokal* (PDL; Local Development Program).⁷ The PDL had been initiated in 2004 to respond to a medium-term policy priority of territorial decentralisation. The program was piloted under the aegis of the then *Ministério da Administração Estatal* (MAE; Ministry of State Administration), through building local capacities for administration and political representation, and was subsequently scaled up to all districts.⁸ The PDL’s approach comprised a system of annual formula-driven allocation of block grants, participatory planning, and competitive procurement. Proposals were generated through consultations at the *suku* (village) level, prioritised by multi-stakeholder groups at subdistrict and district levels, and then implemented under competitive tenders and supervised entirely by subdistrict development committees and district representative assemblies (foreshadowing the potential future role of local government bodies in the form of municipalities). While this local development model had been tested in more than 25 countries,⁹ it was, at the time, perceived by government to fall short in several ways. It was believed that PDL’s exhaustive participatory planning,

6 The issue was not just that one in three Timorese were living in poverty, but the results of the Survey of Living Standards revealed a sharp increase in poverty between 2001 and 2007 (World Bank 2008).

7 It was supported by the UN Capital Development Fund, through funding from the governments of Ireland and Norway.

8 This was not Timor-Leste’s first experience in decentralised spending. A prior experience in community-driven development—the Community Empowerment Program (CEP)—had sought to ‘strengthen local-level social capital to build institutions that reduce poverty and support inclusive patterns of growth’. As distinct from the citizen–state engagement attempted through the PDL, the CEP favoured community allocation decisions, and was distinct from any government administrative artifice. See further, World Bank Independent Evaluation Group 2006. *Implementation Completion Report Review: East Timor Community and Local Governance Project*.

9 www.uncdf.org/node/325.

competitive tendering and elaborate expenditure controls would hinder the pace of spending and could not be scaled to a national operation as quickly as needed. It was also felt that competitive tendering would favour existing contractors, and weigh against the priority of favouring new entrants, such as the veterans. Finally, it was simply ‘too donor driven’, when the premium was on electoral claiming through a modality that was distinctively Timorese in conception and operation.

When the *Pakote Referendum* was announced—two years after the AMP Government took office and within a year of attempts on the lives of the prime minister and president—its proponents argued it would have several advantages over the PDL arrangements. It would reduce time and cost, capitalise a new class of contractors, and quickly deliver infrastructure nationwide. The political signalling could not have been clearer, although significant critiques of the *Pakote Referendum’s* efficacy continued. Whereas PDL had a total annual budget at the time of US\$3 million, the *Pakote Referendum* was allocated US\$70 million in 2009, and nearly US\$150 million would be allocated over the next three years in its subsequent iterations.

Figure 8.3 PDD and PDL budget compared to public overall and capital spending (US\$ millions).

Source: World Bank 2014: 4.

Once the immediate purposes of *Pakote Referendum* had been served, the government made a number of modifications to respond to criticisms about its governance arrangements and efficacy.¹⁰ In 2010, under PDD, new agencies were created at national and sub-national levels (most significantly the *Agencia Nacional do Dezenvolvimento* (National Development Agency)) and refinements were introduced to how projects were planned, and contractors selected and supervised. The *Kommisaun Dezenvolvimentu Distrital* (District Development Commission)¹¹ was made responsible for planning and contracting, and supervising contractor performance. Between 2009 and 2012, the rules governing sub-national spending changed frequently and rapidly—from the radical ‘market devolution’ of 2009, to a mix of centralised planning and decentralised implementation in 2010 and 2011, to some degree of decentralised planning but a greater degree of central control over implementation in 2012. Over this short period, there has also been a rapid consolidation of several sub-national spending systems under the 2012 *Planeamento de Dezenvolvimentu Integradu Distritál* (PDID; Decree Law for Integrated District Development Planning), the PDL, and a new community-driven development program called the *Programa Nasional Dezenvolvimentu Suku* (PNDS; National Village Development Program). PDID ‘defines the rules and regulations applicable on competency, planning, implementation and financing of state projects at the district and sub-district levels’.¹²

10 The Head of Parliamentary Committee G, Pedro da Costa of the ruling party, CNRT, was cited in *Suara Timor Lorosae* as saying the referendum projects lack quality and the committee therefore ‘has asked the government to establish a system of supervision, monitoring and oversight in order to guarantee good works result’. (*Suara Timor Lorosae* 22/12/2009. Referendum Package Lacks Quality. www.etan.org/et2009/12december/31/22referendum.htm). Earlier, on 18/11/2009, the speaker of the national parliament was quoted in *Jornal Nacional Diario* (quoted in FRETILIN 18/11/2009. Gusmão’s Financial Management Questioned from Within. Media release. groups.yahoo.com/group/ETSA/message/9286). The main opposition party, FRETILIN, issued a media release in which the party’s Vice President, Arsenio Bano, called the package ‘a big disaster’ (FRETILIN 27/10/2009. Audit Reveals Gusmão Government’s Woeful Financial Management: Action Looms on Referendum Package. Media release. easttimorlegal.blogspot.com/2009/10/fretilin-media-release-audit-reveals.html). The media release of FRETILIN cited all the criticisms of the package from AMP members of parliaments (MPs) and Timorese academics about project quality under the package. A local civil society organisation, *La’o Hamutuk*, states in its 2010 budget submission that *Pakote Referendum* was ‘opening up avenues for corruption, waste and poor quality, it prevents proper accountability and sustainability for public works infrastructure projects, which are definitely needed by our people’ (*La’o Hamutuk* 18/11/2009. Gusmão’s Financial Management Questioned from Within. Media release. groups.yahoo.com/group/ETSA/message/9286).

11 *Kommisaun Dezenvolvimentu Distrital* comprised the district administrator, subdistrict administrators, representatives of line ministries at the district, and *suku* chiefs.

12 PDID Decree Law, Art. 1(1).

Figure 8.4 Sub-national spending in Timor—a chronology.

Source: World Bank 2014: 7.

The sub-national spending study

The World Bank collaborated with several government ministries in 2012–13 to undertake a comparative evaluation of sub-national spending programs. The prime purpose was to contribute to ongoing efforts to define sub-national spending systems and procedures. It was also intended to speak to political audiences (Timor’s parliament and executive, and the donor community) and spark a wider policy and academic discussion about the role of public finance in consolidating elite settlements in the aftermath of violent conflict.

In essence, these policy and academic discourses raise two questions in common. First, in the aftermath of conflict, under what circumstances do elites invest in institutions to order power and what forms do these institutions take? Second, how do these choices to invest in particular forms of institutions impact on the durability, nature and legitimacy of political settlements? Two aspects of these choices appear to be particularly important in determining the scope, depth, and thus durability of a ‘successful transition’. One is the ability of elites to impose centralised arrangements to collect and distribute rents (Khan 2010; Slater 2010). Another aspect is the ‘ability of central actors and the modalities they use to project authority and distribute resources to places where people live, including them in the settlement by delivering public safety, services, livelihoods and other opportunities’ (Craig and Porter 2014). We believe Timor’s experience with sub-national spending could be helpful in thinking through these issues.

To address the study’s prime purpose, a multidisciplinary team of World Bank staff and consultants and Ministry of Finance officials adopted a ‘mixed methods’ approach. The team analysed databases on total spending through the PDL and *Pakote Referendum*/PDID mechanisms (2005–13); visited the districts of Baucau, Ermera, Bobonaro and Ainaro (and eight subdistricts); and closely examined a representative range of 22 projects. While chosen to be indicative of the

larger picture, the sample for detailed analysis is small, and the results should be approached with due caution. Wide-ranging consultations were held with district and subdistrict administration and line departments, *sukus*, contractors, users of the facilities, non-government organisations (NGOs), and Dili-based government officials. The study provided a comparative analysis of PDD and PDL across five key dimensions:

1. expenditure priorities (rates of budget execution, patterns of spending including links with poverty and geography, achievement of different policy priorities)
2. quality of the assets created (construction standards, durability, 'useability')
3. impact on employment (quantum, quality and equity of opportunity)
4. impact on local contractors and private sector (including short-term and likely medium-term benefits)
5. governance (local stability, disputation, elite capture or inclusivity).

Findings in summary

The full study (World Bank 2014) can only be summarised here. PDL and *Pakote Referendum*/PDD achieved similar results in expenditure priorities and job creation, but diverged considerably on other areas of comparison, such as the quality of infrastructure, the creation of new contractors, and governance-related matters. This is not surprising; each of these mechanisms and the form they took at various times were designed to serve somewhat different priorities. These policy priorities were frequently in tension—at any point in time, one could be ascendant in the minds of policymakers depending on specific political economy considerations.

Table 8.1 Budget execution rates of sub-national as compared to central government investment programs.

	2009	2010	2011	2012
Sub-national programs				
PR/PDD	67%	80%	94%	70%
PDL	93%	103%	98%	99%
Central government				
Government—all capital dev't	85%	86%	81%	46%
Education—capital dev't	n/a	n/a	67%	n/a
Health—capital dev't	n/a	n/a	47%	n/a
Roads—capital dev't	n/a	n/a	27%	n/a

Source: World Bank 2014: 9.

Figure 8.5 Budget execution measures, 2009–12.

Source: World Bank 2014: 10.

Table 8.2: Investment sample—efficiency, quality and useability.

	Total	PDD	PDL
Sample size (n)	19	13	6
Delivery time			
Within year	13	7	6
Extended to next year	3	3	0
Still not completed	3	3	0
Constructed quality			
Acceptable	11	6	5
Barely acceptable	5	4	1
Poor	3	3	0
Useability			
Useable	11	6	5
Partly useable	3	3	0
Not useable	5	4	1

Source: World Bank 2014: 11.

Compared with other government arrangements for capital spending, PDL and PDD both fared very well in terms of *budget execution* and performed considerably better than the rates of execution recorded before 2009—or even now—by most line ministries for infrastructure spending. Spending patterns were broadly (but not entirely) consistent with those for public services prioritised in the government's *Strategic Development Plan* (education, water, health, and agriculture).

Geographical spending equity (measured in terms of dollars spent per capita) under the PDD varied greatly across districts, with the most favoured districts receiving between three to seven times more than the least favoured. No relationship was found between spending patterns and relative need, as captured by poverty head counts—for instance, high per capita allocations were received by Lautem district (with a relatively low poverty rate), whereas low allocations were received by Ainaro (with a relatively high poverty rate).

Table 8.3 PDD allocations per-capita by district (US\$ per capita).

Districts	POPn	PR 2009	DDP 2010	DDP I+II 2011	DDP I+II 2012	Total 2011 & 2012
Aileu	45,724	n/a	29	45	63	108
Ainaro	62,407	n/a	24	37	51	88
Baucau	113,748	20	25	18	34	52
Bobonaro	93,787	37	33	29	41	70
Covalima	62,764	51	n/a	63	66	129
Dili	212,469	31	16	24	29	53
Ermera	118,671	15	n/a	12	29	41
Lautem	65,349	33	36	86	45	132
Liquica	69,925	20	31	50	50	99
Manatuto	41,217	57	49	82	87	170
Manufahi	53,995	44	21	40	72	112
Oecusse	67,736	36	23	35	68	103
Viqueque	72,950	40	33	61	75	137
Totals/Means	1,080,742	35	29	39	48	86
Standard Deviation		12.59	8.58	22.17	18.01	36.44
Highest x Lowest		2.90	3.00	7.00	3.00	4.00

Source: World Bank 2014: 12.

As might be anticipated, technical quality and project completion were more robust under PDL than PDD. With the previously mentioned caveats about the small sample size, the quality of PDD investments is mixed: just under half of projects are of acceptable standard and of benefit to users; three exhibit varying degrees of design, construction quality, and usability problems; and four are not usable for the intended purpose without additional investments. A follow-up study of a larger sample was about to commence at the time of writing.

While neither was a specialised labour creation program, the *employment impact* of both PDL and PDD was modest. Compared to the large public works rural investment programs in Asia—such as that established by the National Rural Employment Guarantee Act in India—the share of total investment costs going to unskilled and skilled labour payments under PDD and PDL are low at around

6.5 per cent and 3.5 per cent respectively (specialised labour creation programs range between 50 and 75 per cent). The employment impact depends greatly on the type of infrastructure or investment scheme (for instance, buildings generally employ much less labour than irrigation schemes and erosion protection walls). The programs provided seasonal employment to an estimated 2.5 to 10 per cent of the subdistrict workforce,¹³ and it was predominantly the rural underemployed who benefited. Significantly, the benefits were mainly local, and shared widely. For the poorest households, the additional cash injection is a significant proportion of household income.

Discounting the considerable numbers of ‘briefcase companies’,¹⁴ *Pakote Referendum/PDD* appears to have succeeded in creating a capital base and revenue stream for a *new class of contractors*. The number of registered local contractors has expanded greatly, in the order of a threefold increase since 2009, and a large number of these contractors were each year awarded a PDD contract. However, the fact that contractors were precluded from winning more than one project per year meant there were few opportunities and incentives for contractors to consolidate their businesses and diversify over time. Thus, the expansion in domestic contractor capacity may prove to have been more apparent than real—clearly, a longer time frame and more extensive case analysis would be needed to draw conclusions here.

The *governance dividends* of sub-national spending were mixed. On the one hand, these programs enabled large numbers of Timorese to participate in the allocation of public resources and the production of assets largely in accordance with their priorities. Sub-national spending is best seen as part of a suite of measures the government introduced to support its political, stability and social objectives. Thus, while the way in which these programs enabled government to target important constituencies needed to build stable political settlements should not be underestimated, it would be premature to be conclusive. The *Pakote Referendum/PDD* programs have helped to distribute wealth to rural areas—benefiting a number of constituencies to whom the government wanted to deliver a share of the oil wealth. Nowhere is this more apparent than in the geographical allocations; when the district/per capita allocations are overlaid with a political ‘mapping’, the pattern of spending is more explicable—an astute use of spending to assuage potential spoilers, broaden political coalitions,

13 Extrapolations for FY12 Timorese financial year is the same as their calendar year, suggesting that these programs have created some 1.2 million unskilled and 220,000 skilled workdays respectively. At subdistrict level, this could provide 165 persons with 100 days of employment each, or 740 persons with 25 days each (World Bank 2014: 13).

14 Briefcase companies refer to those that have little by way of capital and no operating site. In the current context, they refer to companies that were awarded contracts and went on to ‘on-sell’ the contract to contractors with the requisite capacity, taking a percentage of the contract price.

manage dissent in relation to such initiatives as the south coast development, and part of a strategy to win 2012 elections and fracture the unity of the political opposition.

On the other hand, nine out of 13 PDD projects examined closely gave rise to some form of dispute about land, procurement, labour or contractor performance, whereas only one of the six PDL projects gave rise to a dispute (contractor-related). No evidence was found to support the view that sub-national spending mechanisms, compared to centralised spending by line ministries, are vulnerable to 'weak local capacity'. The reasons for variable outcomes are more complex. They lie in the need to frequently modify systems and procedures in response to changing priorities and lessons learned. Several aspects of poor performance may be mitigated in ways anticipated by the PDID Decree Law 2012, including the clarification of assignments of responsibilities (in relation, for instance, to certification and supervision) and by more consistent attention to public communication and accountability arrangements.

The study concluded that, after experimenting with a range of innovative but risky arrangements to deliver public spending and address a series of economic, social and political priorities, the government had largely achieved the initial objectives of *Pakote Referendum*/PDD. It took the decision to 'regularise' the system through the PDID Decree Law 2012 as the point of departure to make several recommendations, including in respect of how budgets are allocated to districts; measures to 'incentivise' better performance; simpler contractor pre-qualification procedures, and competitive tendering to improve contractor performance and create significant cost savings; and reverting to district payments for contractors to break the highly problematic payment bottleneck arising from delays in certification reporting to Dili and in central Treasury payments. Since the study was completed, many of the report's recommendations have been adopted (including competitive tendering and predictable, formula-based budget allocations) or are in the process of being implemented through revisions to the PDID Decree Law. In view of the study's limited sample, government has initiated a further round of analysis of both the quality of assets and the PDID systems and procedures; this will include a study sample of around 200 investment projects.

Broader lessons: institutions for re-ordering power in post-conflict contexts

This chapter has drawn on several empirical sources: new qualitative research; existing data and research on public expenditure (including on the wage bill, large infrastructure spending, an expanded social protection scheme, goods and

social services spending); and a broader review of literature. But in drawing wider lessons, it must be noted that the study of sub-national spending on which this chapter draws provides only a thin basis on which to sustain conclusions about how sub-national spending may be transforming the country's political economy.

At face value, Timor-Leste appears to provide a positive example of where domestic elites have used the 'breathing space' given by a peacekeeping operation to forge a locally acceptable settlement that has been sustained hitherto after the departure of foreign troops and police (Akmeemana 2014). The approach that was adopted was politically savvy, targeted at particular constituencies, but also the broader populace. Although the United Nations Integrated Mission in Timor-Leste assumed executive policing responsibilities with one of the largest UN police contingents in the world from 2006 until 2011, the Timorese police force has answered to its own command since 2008 and handled internal threats itself (ICG 2012). In the interplay between a government buoyed by large inflows of petroleum revenues, and a UN mission with a very broad mandate, a settlement with a distinctively East Timorese cast emerged, into which the UN had difficulty in inserting itself (Goldstone 2013: 209–10); but it was one that was locally legitimate, and has thus brought at least near-term stability. A striking characteristic has been the government's ability to reach and 'cater to groups which see it as the focal point for their demands for various forms of recognition (material, political, and symbolic) to which they feel entitled as compensation for losses sustained or services rendered during the struggle for independence and since' (Goldstone 2013: 209). The argument that Timor has moved from a very narrowly based elite bargain in the direction of a more inclusive settlement does not deny that a new economic elite is capturing the bulk of resources in the post-2007 era.

Certainly, the ways in which public spending can be adroitly used to create political capital, pacify populations and consolidate alliances by demonstrating 'commitment credibility' have been well documented, as have the failures to do so and their consequences in the form of violent conflict (Taydas and Peksen 2012; Azam 2001: 435; Burgoon 2006). Recent observers of public spending in Timor-Leste conclude that it 'seems to be enriching elites to a greater degree than before, which is also in line with the expectations of particularist rent distribution associated with clientelist rentier states' (Barma 2014). This may be true, but in respect of the particular case of sub-national spending, this conclusion needs to be nuanced. Certainly, the pace and frequency of changes to sub-national spending arrangements generated confusion and scepticism among officials, local leaders and common citizens. Yet it also provided incentives for certain disaffected groups to co-operate, and thus, while amounting to only 3 per cent of the budget, it has had a much larger political footprint of

immediate social and electoral dividends for the incumbent government. It has also arguably underwritten a political assessment that a blend of centralisation and decentralisation offers technically feasible and politically credible ways to consolidate power and project authority to dispersed rural populations, while building upon existing community governance arrangements (which shape social order and collective values for the majority rural population) in order to achieve stability.

Second, the PDD mechanism certainly generated a fair number of localised disputes. This is hardly surprising given the pace of roll-out; the frequent changes in the rules, often year on year; the sheer logistical difficulties of monitoring up to 500 ongoing projects each year; and the fact that local authority figures were largely removed from the process. The comparative evidence from PDL points to the obvious dividends of local participatory processes, of companies prevailing through competitive tendering, and of having local authorities involved—reduced disputes around land, creating incentives for better performance by contractors, and greater local ‘ownership’ of both process and product.

We would caution against overstating either positive spillover effects of PDD mechanisms, or pessimism that they foster forms of patronage that corrode democratic prospects. The claims that decentralised spending mechanisms are socially generative, including those that invest heavily in popular participation, are routinely overstated and decidedly mixed;¹⁵ there is seldom evidence of positive long-term impact on institutional quality, inclusiveness of decision-making, trust and group formation (Casey et al. 2012; King 2013). On the other hand, the disputes generated by these mechanisms are not necessarily corrosive in the long term, provided that they do not feed larger narratives of grievance and exclusion.¹⁶ Decentralised spending arrangements undoubtedly multiply the number of sites where political contest occurs. But, while these contests might result in small disputes, the overall project that creates local contests about where budget should be spent, by whom and with what expectations can also be a powerful form of political legitimation for the governing regime.

The sub-national spending study—on the basis of limited case examples—did not find that the distribution of benevolent largesse by the state necessarily accentuates existing cleavages. Admittedly, Timor’s local landscape is quite different from that in any number of countries emerging from civil war. Social cohesion at the local level is fairly high; local norms generally act as some form of constraint on elite behaviour; and prevalent cultural ideals and

15 See King (2013) on the comparative record of community-driven development projects in Afghanistan, Democratic Republic of Congo, Aceh (Indonesia), Liberia and Sierra Leone.

16 Belun’s *Conflict Potential Analysis* reports a ‘medium level’ conflict potential, ‘attest(ing) to the gradual stabilisation of the security situation’ and, of interest, ‘an overall improvement in most indicators describing politically motivated violence’ (Belun 2013: 5).

expectations of leadership emphasise community co-operation and have enabled cultural continuity and survival through occupation, hardship, natural disaster, and political upheaval (Brown 2012a: 66; 2012b). Moreover, many of the kinds of conflicts observed around sub-national spending could be ameliorated by measures recommended by the study and appear to have been largely adopted (although their remedial impact is yet to be determined). Further, had it been the case that sub-national spending was projecting political power that was perceived as inequitable, and thus creating cleavages or feeding existing narratives of exclusion, this possibility must be seen against the increased vote achieved by the prime minister's CNRT (*Congresso para a Nacional de Reconstrução de Timor*; National Congress for Timorese Reconstruction) party in the 2012 elections—for the first time, it had a higher primary vote than FRETILIN (*Frente Revolucionária de Timor-Leste Independente*; Revolutionary Front for an Independent East Timor)—and commitments by government to further ensconce these arrangements.

While we cannot claim insight into the political strategy of Timor's leaders, it does appear that they are favourably weighing the political and electoral dividends of sub-national spending to date. Since the 2012 PDID Decree, the government has committed a further US\$300 million over eight years to a national, village-level spending program in the PNDS, and announced a further, perhaps expanded, round of sub-national spending under revisions to the PDID Decree from 2015. Perhaps more significantly, the Council of Ministers approved the Decree Law on Pre-Deconcentration in August 2013, a new law is being prepared to govern village authorities, and elections for district/municipal assemblies and village councils are anticipated for 2015 and beyond. Looking forward, however, it would be foolhardy for observers to assume that Timor-Leste is set to 'institutionally innovate' along a path toward a liberal form of decentralised government.

Timor's record of fast-tracked, dynamic institutional innovation around sub-national spending mechanisms should interest proponents of 'iterative, adaptive learning' (Andrews 2013). This is instanced by the *Pakote Referendum's* radical break with convention, the experimentation with hybrid institutional forms, the circling back and forth between decentralised and centralised authority across different elements of the system, through to the routines of administrative rationality suggested by the PDID Decree and the revisions that are currently being drafted. This record also speaks to the conditions under which governing elites will invest in innovative arrangements that break from the past to enhance prospects of regime durability. But, in neither form nor function do these institutional modalities mimic liberal conventions about the desirability of particular models of government at local level.

Conclusion

The current PDID mechanism is a hybrid system that resonates with the broader re-ordering of power in Timor-Leste. It is populist in character, and demonstrably shifts discretion over some aspects of public finance management to lower levels of territorial authority. At the same time, the variable geographically and politically targeted nature of spending points to the salience of a highly centralised political executive (in the form of the annual Budget Review Committee process). It is reliant on capabilities that are alert to and adept in the political art and value in making decisions right down to the project level, on the basis of relationships with local authorities, officials and other targeted constituencies. In light of the experience with *Pakote Referendum*/PDD, the Pre-Deconcentration Decree Law is unlikely to herald a linear trajectory to populist devolution and participatory democracy, but rather its essence will be the extension of the regime's reach into the periphery. With the PNDS also comes the acknowledgement of the *suku* as a point of articulation between locally established governance practices and efforts to render national socio-political order 'legible' from the centre (Brown 2012a: 61).

How do elite choices to invest in particular forms of institutions impact on the durability, nature and legitimacy of political settlements over time? Is the system emerging in Timor-Leste what Terry Karl describes as a 'rentier' system that 'progressively substitutes public spending for statecraft'? (Karl 1997). There might, in closing, be two contending answers to this question. In the specific and narrow terms of the study reported here, one answer may lie in whether political elites follow through on a few key principles—local consultation, competitive procurement, expenditure transparency, and so on—to which they have apparently committed in the PDID Decree. A second, much more speculative response may be found in the wider literature of comparative politics (Slater 2010) and historical institutionalism (Thelen 2004), together with scholarship on the oil curse (for example, Karl 1997; Barma 2014). This might suggest that the flow of oil rents will undermine incentives for elites to coalesce and invest in functional and legitimate public authorities. Among other things, this would mean that follow-through on principles like transparency and competitive procurement might be likely in form, but not in function. Rather, oil will finance what Slater calls a 'provisioning pact', which may be sustained over time; but, over time, the political demands perpetuated by provisioning will exceed available revenue and seriously corrode state capacity (Slater 2010). According to Slater, this trajectory leads to either fragmentation or militarisation (armed groups in control). Such a trajectory might prove to be both crisis-prone as elites battle for control over the prize of oil rents (Tornell and Lane 1999).

and, for a time, durable.¹⁷ Durability would rest on two capabilities: patronage through state-sanctioned systems (such as the PDD and PNDS), and coercion to deal with episodic conflict.

The type of system we describe as developing in Timor-Leste faces two key vulnerabilities. Leadership transitions are difficult in systems that are highly dependent on a personalised executive. As with the regimes of Kagame (Rwanda), Museveni (Uganda), and Hun Sen (Cambodia), government since 2007 has been highly dependent on the personalised authority of Prime Minister Gusmão. The first real test of the emerging political settlement and ‘mutual dependency’ among elites (Phillips 2013) will occur now that the Prime Minister has stepped down. There are clear signals that the transition has been given a great deal of thought. In the 2012 elections, CNRT successfully thwarted FRETILIN’s attempts to recapture popular support in the rural base. After the election, it appeared that the FRETILIN leadership, and its Secretary-General Mari Alkatiri in particular, has negotiated a form of ‘détente’ with then Prime Minister Gusmão. This has been described by some as the beginning of a ‘post-political’ era in Timorese politics, in which Gusmão and Alkatiri have elected to eschew direct political competition in favour of a form of collaboration, and a consolidation of the patrimonial system (Rees 2013). The second vulnerability is structural: the exhaustion of oil and gas revenues. If the economy does not diversify in the medium term, the country’s economic viability will be in question unless new hydrocarbon deposits are found, and may need to be buttressed by significant international interventions—sizeable aid rents along with potential security interventions—in the longer term.

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17 Timor-Leste is by no means unique in this scenario. It has become a well-established feature of oil states that while they develop coercive and redistributive capabilities, the general trajectory is both ‘crisis prone’ and ‘durable’. See Peterside et al. (2012).

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