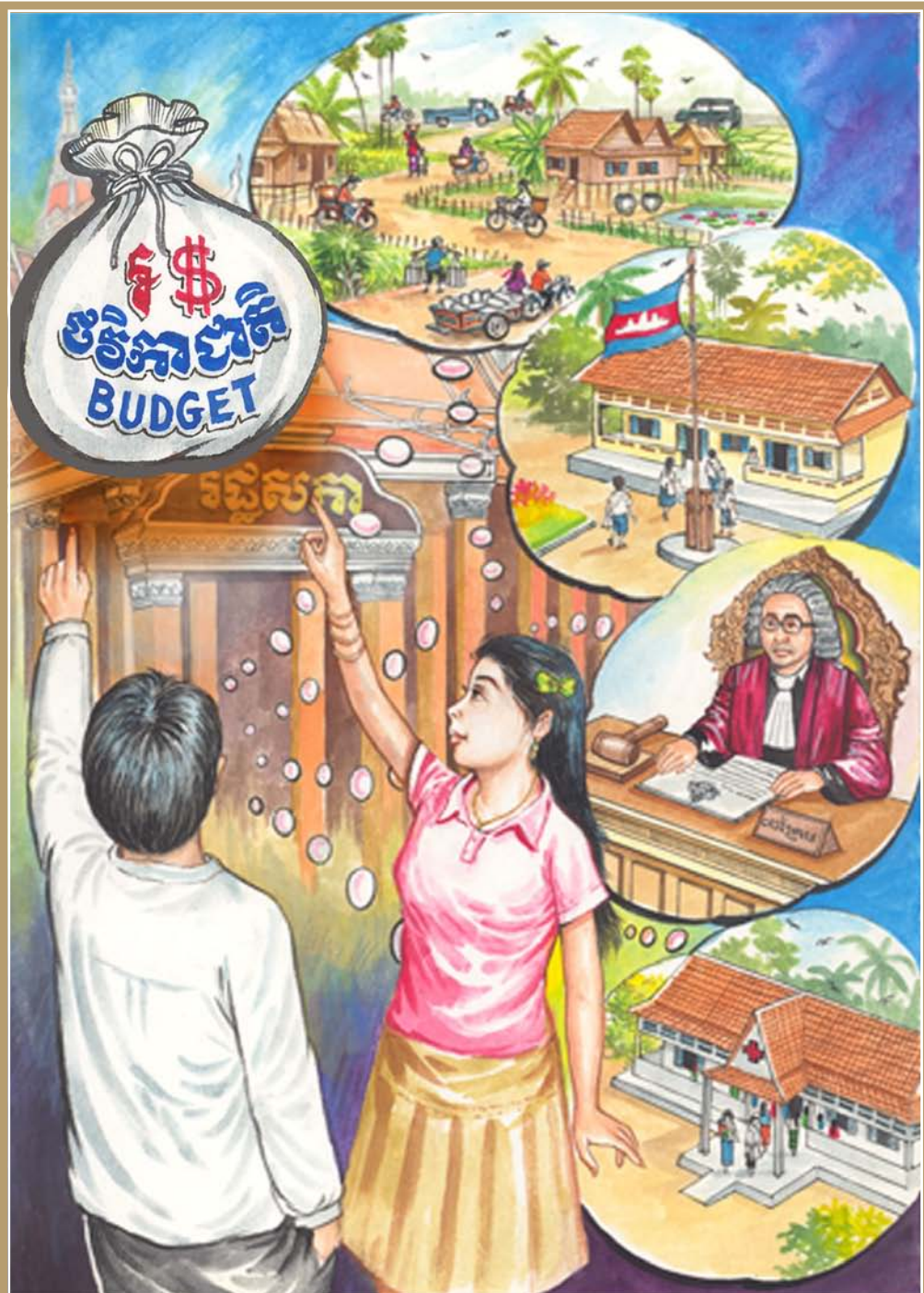


# GUIDE TO THE NATIONAL BUDGET



## ACKNOWLEDGEMENTS

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# **GUIDE TO THE NATIONAL BUDGET**

Phnom Penh, November 2007

**THE NGO FORUM ON CAMBODIA**

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## List of Acronyms and Abbreviations

ADB	Asian Development Bank
CC	Commune Council
CR	Cambodian Riel
CMDG	Cambodia Millennium Development Goals
D&D	Decentralisation and deconcentration
EIC	Economic Institute of Cambodia
GDP	Gross Domestic Product
EITI	Extractive Industries Transparency Initiative
EI's	Extractive Industries
IDA	International Development Association
IMF	International Monetary Fund
MEF	Ministry of Economy and Finance
NA	National Assembly
NAA	National Audit Authority
NGO	Non-Governmental Organisation
NGOF	The NGO Forum on Cambodia
NSDP	National Strategic Development Plan 2006-2010
PFMRP	Public Financial Management Reform Program
RGC	Royal Government of Cambodia
US\$	United States Dollar





## 1 Introduction

The Royal Government of Cambodia (RGC) is a large and complex financial institution. Every year, it raises and spends hundreds of millions of dollars. This money comes from taxes, fees and fines, donor aid, and a variety of other sources; it goes towards the operations of government: paying civil servant salaries in ministries, schools, hospitals and police stations, for example, and investing in roads and irrigation, etc. In short, how this money is raised and how it is spent affects everyone in Cambodia.

Who is in charge of these hundreds of millions of dollars? Ultimately, we, the citizens of Cambodia, are in charge. Cambodian citizens exercise control by taking part in elections; the elected government makes crucial decisions on our behalf. However, outside the election process, citizen involvement in the annual budget process is currently limited. More participation in the budget process should lead to a more direct link between government spending and the realization of the needs, desires and aspirations of Cambodian citizens. It would also lead to a deeper understanding of democracy and the role that Cambodian citizens can play to hold the government accountable.

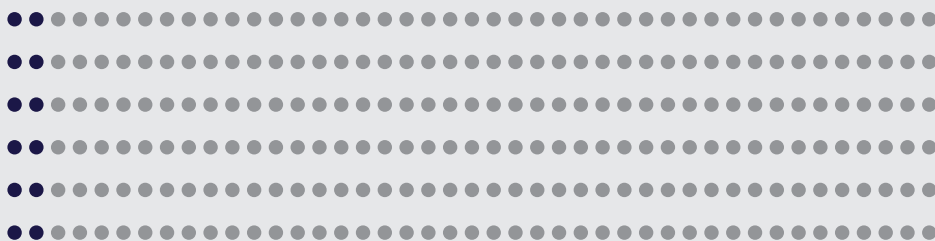
Knowledge on the National Budget, the budget cycle and trends in revenue and expenditure rests only with a small number of specialists in government, the National Assembly, Senate and research institutions, and among development partners. Although a large number of laws and technical articles exist, there is no single resource offering complete information about the budget and the budgetary process. This Guide aims to fill this gap and is intended to be a useful resource for everyone directly or indirectly involved with the National Budget, including government officials, members of parliament, media professionals, university lecturers and students, NGO staff, and all other Cambodian citizens. By using this Guide, it is hoped that all these stakeholders will be able to find a space for themselves in the budgetary process and to make their own contribution to a constructive debate about the National Budget.

This Guide is structured as follows: Chapter 2 defines the National Budget, describes its importance and provides details on the different types of revenue and

expenditure, on how the National Budget Law presents this information in its tables, and the ambitions government has for its National Budget as outlined in the Public Financial Management Reform Program. Chapter 3 describes the different stages of the budget cycle, the timelines, and the institutions involved in the process and their activities. Chapter 4 gives an overview of trends in revenue and expenditure in the national budgets of 2000 to 2006, as well as trends in interest payments and debt amortization for this period. Chapter 4 continues with an assessment of the effect of the National Budget on poverty reduction and provides an overview of issues related to decentralization and deconcentration (D&D) as well as issues related to public debt. The final chapter of the Guide looks at current pertinent issues, such as access to budget-related information and anticipated future revenues from the natural resources of oil, gas and mining.

Annex 1 contains a list of explanations of the key technical terms used in this Guide. Annex 2 provides an overview of reading material and websites on the Cambodian National Budget, on relevant laws and on other data, as well more general information on public finance. Annex 3 and Annex 4 provide tables giving detailed data on trends in the National Budget from 2000 to 2006, as well as tables giving detailed excerpts from the 2007 National Budget Law for those who would like to have immediate access to some of the data available.

This Guide is part of the broader effort of the NGO Forum's budget project which aims to generate a constructive, and evidence based, dialogue between Civil Society Organisations and the Executive and Legislative branches of the Royal Government. Suggestions and comments on this Guide, as well as requests for further information can be sent to the NGO Forum's budget project at the address printed on the back of this Guide.



## 2 THE NATIONAL BUDGET

### 2.1 What is the National Budget?

The national budget is a statement of government's planned receipts and expenditures and allows the government to determine whether it has enough money coming in to meet its expenses. The national budget gives authority to the executive to collect revenues and spend this in order to achieve government's objectives such as poverty reduction and economic development. The budget is the most potent instrument of the government in carrying out its policies.

In Cambodia, the National Budget is prepared every year for implementation during the next calendar year (which coincides with the fiscal year). The National Budget is prepared by the government and needs to be approved by the National Assembly and the Senate before implementation. After receiving legislative approval, the National Budget becomes law.

### 2.2 Importance of the National Budget

Budgeting is an integral part of society. In today's busy and challenging world, we budget our time, our food, our clothes and our entertainment, etc. In the case of limited resources or money, budgeting should help ensure that money is spent in an effective manner. By using a budget, we can know in advance how much income we will be able to obtain, and how much we can spend on certain priorities over a certain period of time.

In the same way, the government uses the National Budget as a planning tool for revenue mobilization and to determine expenditures to meet development needs. A well prepared budget, one which reflects the country's socioeconomic policy priorities, will allow the government to achieve its poverty reduction and development goals.

In short, the budget of a country affects everyday lives and the future of whole society as a whole. Decisions on budgeting have an impact on all economic and social activities, ranging from the place we live, the place we work, the means of transport we use, the healthcare and education we can access, and the safety, sanitation and

utilities we can enjoy.

## 2.3 Structure of the National Budget

In Cambodia, the National Budget is prepared for government operation during the following fiscal year. The National Budget Law has three main parts:

- Revenues;
- Expenditures; and
- Deficit.

### 2.3.1 Revenue

The government raises revenue from various sources in order to fund government activities and development programs. These revenues are divided into current revenues and capital revenues. In 2007, the government committed to collecting domestic revenues to the total amount of CR3,282,173 million (US\$797.6 million), of which current revenues are CR3,252,173 million (US\$790.3 million) and capital revenues are CR30,000 million (US\$7.2 million).

Tax and non-tax revenues make up current revenues. Tax revenues are those received from taxes on goods, service and international trade. Examples include personal income tax, profit tax, excise on casinos, property tax, custom duties, value-added tax (VAT), and tax on export of timber. In the 2007 Budget Law, the government aims to collect tax revenues to the total amount of CR2,682,000 million (US\$651.7 million). The target for non-tax revenues for 2007 is CR570,173 million (US\$138.5 million). This includes revenues from renting and sale of public property, mining concessions, public enterprise profits, privatization, passport and visa fees, and administrative services.

Capital revenues include domestic capital revenues, mainly from financial investments, and capital revenues from external sources, which are made up of the budget support fund, loans and grants<sup>1</sup>. In 2007, planned total capital revenue is CR1,370,133 million (US\$333 million), of which only 2.2 percent, or CR30,000 million (US\$7.2 million) is domestic capital revenue. The rest is in loans and grants from bilateral and multilateral development partners.

Compared with in other low-income countries, revenue collected by the Cambodian government is very low, averaging only 6.8 percent of GDP during the 1995-2004

<sup>1</sup> Article 7 of the 2007 Budget Law. Before 2007, capital revenues include revenues from the sale of public properties/assets and privatization. However, in the 2007 Budget Law, these revenues are classified as current revenues.

period (the average for low-income countries during this period amounted to 14.2 percent) (World Bank, 2007: 158). However, owing to the many reforms underway to increase revenue collection, this increased to 10.4 percent in 2006 (IMF, 2007). Further, one of the main objectives described in a Circular dated December 30, 2006 of the Ministry of Economy and Finance (MEF) was that the government was committed to collecting revenue amounting to 10.92 percent of GDP in 2007. Many measures are being set up in order to enforce revenue collection, mostly concerning the role of the Customs and Excise Department in the collection of tax revenue, and the collection of non-tax revenue by other institutions. Details on government revenues can be found in Annex 3's Table A (General Government Revenues of the National Budget Law).

### *2.3.2 Expenditure*

Government expenditure is separated into current expenditures and capital expenditures. In 2007, total government expenditure is planned at CR4,522,306 million (US\$1,099 million) (see Table 2.1).

**Current expenditures** refer to the funds used to keep services running on a daily basis. This encompasses salaries of public officials, goods needed to provide services (such as medicines and schoolbooks) and other services. Other examples of current expenditures include social or economic interventions, interest payments and other unexpected expenditures. Current expenditure in 2007 is planned at CR2,837,173 million (US\$689.4 million), showing a nominal increase of 17.5 percent compared with the 2006 budget plan.

**Capital expenditures** include investment for future benefit, financing of investment projects, partnership funds and debt amortization. Examples of capital expenditures include the construction of public infrastructure, such as roads, bridges, electricity grids and telecommunication. In the Cambodian National Budget, the maintenance of this public infrastructure is included in the capital budget. The 2007 Budget Law allocated CR1,685,133 million (US\$409.5 million) for capital expenditure, a nominal increase of 20.4 percent compared with 2006.

### *2.3.3 Deficit*

Deficit shows the difference between government domestic revenue (excluding grants and loans)<sup>2</sup> and total expenditure. If the government has more revenue than expenditure, it is in surplus. On the other hand, if the government spends more

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<sup>2</sup> In the Budget Law, grants and loans are categorized as capital revenues from bilateral or multilateral development partners.

than it collects, there is a deficit. In Cambodia, as a developing economy, the latter scenario is the reality: the government needs to borrow money from the domestic or international capital market to cover this deficit. The Cambodian deficit is financed mostly by development partners, in the form of grants and loans. As shown in Table 2.1 below, for 2007, the government expects to collect as current revenue a little more than the expected current expenditure, causing a surplus current budget at CR415,000 million (US\$100.8 million). However, taking into account the capital budget, Cambodia will experience a deficit of CR1,240,133 million (US\$301.3 million). This deficit is being financed by external sources – mostly development partners, both bilateral and multilateral – in the form of loans and grants.

**Table 2.1: Structure of the Cambodian National Budget (2007)**

State financial transactions	Amount	Surplus(+)/ deficit (-)
<b>I. Domestic revenue</b>	3,282,173	
1. Current revenues	3,252,173	
2. Domestic capital revenues	30,000	
<b>II. Total expenditure</b>	4,522,306	
1. Current expenditure	2,837,173	
2. Capital expenditure	1,685,133	
▪ Domestically financed public investment	575,133	
• Budget funded	345,000	
- Investment projects	220,000	
- Counterpart fund	125,000	
• Investment by budget support fund	230,133	
▪ Externally financed public investment	1,110,000	
Surplus of current budget (I.1 – II.1)		415,000
Deficit of general budget (I-II)		(1,240,133)
<b>III. Financing</b>		1,240,133
1. External financing		
▪ Budget support fund		230,133
▪ Direct external public investment fund		1,110,000
▪ Loan payment		(100,000)
2. Domestic financing		
▪ National Bank financing		

**Source:** *National Budget Law (RGC, 2007).*



When financing is in the form of loans, the government needs to pay interest, as well as loan repayment in the future; this payment is a contractual obligation. This means that the government must provide for paying interest on its debt and debt amortization before it budgets for other expenditures. It also means that, at some point in the future, the amount of the loans, and not only their interest, will have to be repaid.

### 2.3.4 Presentation of the National Budget

One important feature of the Cambodian National Budget is its dual nature. This means that current expenditure and capital expenditure are presented separately, as outlined in the description of the different tables in the Budget Law. In the 2007 Budget Law, a first step has been made in terms of the presentation of the National Budget, in the sense that a pilot test on program-based budgeting has been introduced. A program is formulated as a set of activities which intends to contribute to an identifiable government objective and which has defined what the expected results are and how these can be evaluated.

For the year 2007, this pilot is based on the implemented Priority Action Programs (PAP), starting with the seven priority ministries. The fund for program budgeting for 2007 is planned at CR396,225 million (US\$96.2 million) or around 14 percent of the total current budget. This total amount is distributed among the seven ministries and represents only a small amount of each ministry's total budget to covers its certain priority programs. Although individual programs are not included in the tables of the 2007 Budget Law, an overview of the amounts involved has been provided, as presented in Table 2.2 below.

	<b>Amount in CR (million)</b>	<b>Amount in US\$ (million)</b>	<b>Share of current expenditure (%)</b>
Ministry of Education	125,947	30.8	23.1
Ministry of Health	82,587	20.2	24.5
Ministry of Agriculture	29,632	7.3	18.7
Ministry of Rural Development	16,290	4.0	43.7
Ministry of Land Management and Urban Planning	2,200	0.5	13.7
Ministry of Justice	1,210	0.3	6.4
Ministry of Women's Affairs	860	0.2	5.2

**Source:** 'Context of the Draft Budget Law 2007' (MEF, 2006b).

Annex 2 of this Guide provides a detailed extract of some of the tables from the 2007 Budget Law. Box 2.1 provides a description of the six tables that are part of the National

Budget Law. Table A provides details on state revenues; Table B gives an overview of current expenditure; Tables C1, C2 and C3 look at capital expenditure; and Table D deals with division of capital expenditure between central and provincial/city administrations.

### **Box 2.1: Description of Tables in the National Budget**

- ◆ **Table A** describes in detail state revenue. It presents the total budget revenue (both current and capital revenues, as well as revenues from domestic and external sources). This table lists expected revenues according to group, chapter, account and sub-account. The figures are presented in CR millions. In the 2007 Budget Law, Table A consists of four pages.
- ◆ **Table B** describes state general expenditure. In this table (three pages), the budget amount, both current and capital, is classified by type and separately by ministry at aggregate level of central administration and provincial/municipality. It needs to be noted that this table only provides information on current expenditure; columns for capital expenditures are empty.
- ◆ **Tables C1 and C2** describes in detail the capital expenditure of the state's general budget. These tables list all projects for the different ministries. All projects are listed by project number, and the budget for each project is presented for the next three years. Because this table gives detailed budget figures for all investment projects, it consists of 14 pages. Table C1 presents figures in US\$ (thousands) and Table C2 gives the figures in CR (millions).
- ◆ **Table C3** is entitled capital expenditure of the state's general budget, program credit<sup>3</sup> and committed credit. This is a one-page summary of total capital investment for each ministry CR (millions). It also shows committed credit, which is anticipated capital investment by donors. This committed credit budget is divided into three different categories: i) ongoing, ii) agreed and iii) under negotiation.
- ◆ **Table D** describes capital expenditure of the state's general budget, committed credit and payment credit<sup>4</sup>. This table presents the figures for capital expenditure at the aggregate level in CR (millions). Vertically, this table separates the budget by ministry and divides it into central and provincial/municipal administrations. Horizontally, it shows the budget for public investment separated by funding source, domestic financing and external financing, divided further into committed credit and payment credit. In the 2007 Budget Law, Table D is up of three pages.

<sup>3</sup> Program credit is the total budget for capital investment (funded by both domestic sources and external sources). Committed credit is the budget proposed for external funding from donors; this committed credit is usually off-budget in operation.

<sup>4</sup> Not all the proposed investment programs (committed credits) are expected to be approved. Payment credit is the expected approved budget from the donors.

## 2.4 Aims of the Cambodian National Budget: the PFMRP

In the foreword of the RGC's Public Financial Management Reform Program (PFMRP), which began in 2005, the Prime Minister states that: 'Ultimately, our mobilization, guardianship and deployment of public resources should, over time, yield the best possible results for the benefit of the nation and all of its citizens, especially the poor and vulnerable groups' and thereby stresses the importance of the National Budget for all Cambodian citizens. On its way to completion in 2015, the stated aim of the reform program is to achieve a public financial management system that will approach the highest standards, in the region and internationally. To achieve this, the activities carried out by the government within the PFMRP include working towards a budget which:

- Is **realistic**, which means that it is prepared and implemented as intended in a predictable manner; government expenditures closely follow the allocations in the budget approved by the National Assembly;
- **Reflects the policy priorities** of the RGC which are outlined in the National Strategic Development Plan (NSDP);
- **Captures all fiscal transactions** to which the RGC is legally entitled; and
- Operates in a system where external **financial accountability and transparency** arrangements are operating effectively (e.g. communities have regular access to information on budgets allocated to and funds received by service delivery units; an external audit covers all major public sector entities and conducts a full financial audit).





## 3 THE BUDGET CYCLE

The budget process is not just one event or document, but rather an ongoing process from planning, to resource allocation, to enactment, to implementation, to monitoring of implementation and independent auditing. According to the 1993 Law on Financial System and other applicable norms, the Ministry of Economy and Finance (MEF) plays the leading role in budget formulation. However, other ministries, provincial offices, government agencies and institutions are also involved at different stages, according to their roles and responsibilities.

According to the 2007 Budget Law, the calendar for budget preparation consists of three steps: preparation of strategic plans; preparation of the budget; and adoption of the budget. However, a full budget cycle also includes implementation, monitoring and control, as well as the final stage, which is the audit. The section below describes the actors involved, their activities and the timeline for each stage: i) preparation of strategic plans; ii) preparation of the budget; iii) adoption of the budget; iv) budget implementation, monitoring and control; and v) auditing.

### 3.1 Strategic Plan Preparation (March to May)

This is the starting point of the annual budget process. MEF prepares a macroeconomic framework and the medium-term public financial policy, in line with the national policy framework. MEF takes into account analysis of the current economic and financial situation and its future prospects for the short and medium terms, as well as any macroeconomic constraints. The framework is submitted to the Council of Ministers for approval.

After the Council of Ministers approves the above-mentioned macroeconomic framework and the medium-term public financial policy, MEF issues a Circular as guidance for all ministries and relevant government institutions to prepare their strategic budget plan.

All ministries, government institutions and provincial departments prepare a strategic budget plan based on the guidelines provided by MEF and adjust the plan to

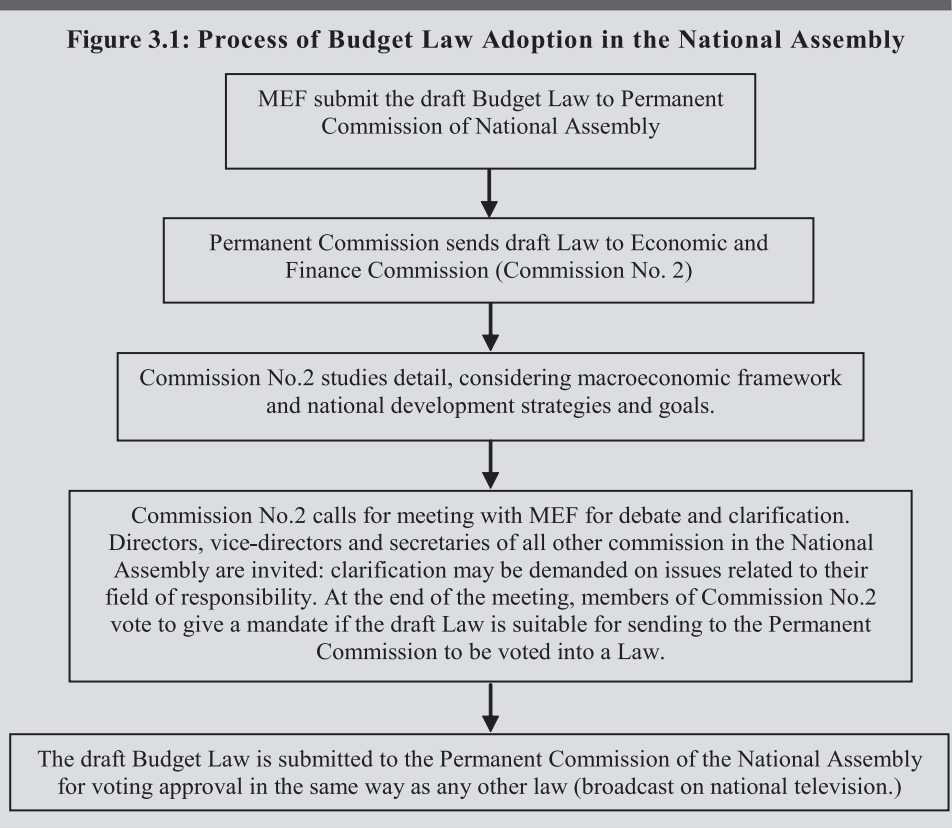
their own vision, goals, objectives and priorities, which should align with sector priorities and the NSDP

### 3.2 Preparation of the Budget (June to September)

At the beginning of **June**, MEF drafts another Guideline on technical procedures for the preparation of sector budgets. This guideline must be adopted by the Council of Ministers by the first week of June. The Guideline is then sent to relevant institutions so they can prepare a detailed budget. With this Guideline, all ministers, directors of independent state institutions and provincial/municipal governors prepare their detailed budgets, for both revenue and expenditure, and submit these to MEF by **July 15**. MEF compiles and adds up all the revenues and expenditures proposed in the detailed budgets.

The month of **August** is devoted to budgetary negotiations. Ministers from all line ministries, directors of all independent state institutions and provincial/municipal governors are invited by MEF to discuss and debate their budget proposals.

In **September**, after discussion and debate, MEF finalizes the balance of revenues and expenditure to the appropriate level. Then a draft National Budget Law is pre-



pared, together with an explanatory note.

### 3.3 Adoption of the Budget (October to December)

According to the 2007 Budget Law, during the first week of October the draft budget is submitted to the Council of Ministers for approval. After checking and endorsing the draft budget, the Council of Ministers submits it to the National Assembly. Submission to the National Assembly must be done in the first week of November.

<b>Table 3.1: New Calendar for MEF to Prepare the National Budget</b>	
<b>March – May</b>	<ul style="list-style-type: none"> <li>▪ Prepare new macroeconomic policy and medium-term public finance framework coherent with the national policy on development, for approval by the Council of Ministers (first week of March)</li> <li>▪ Issue Circular on how to prepare strategic budget plan in accordance with the previously mentioned macroeconomic policy and medium-term public finance framework (first week of April)</li> <li>▪ Ministers, directors of independent state institutions and municipal/provincial governors to prepare strategic plans for own budgets</li> </ul>
<b>June – September</b>	<ul style="list-style-type: none"> <li>▪ Draft Guideline on how to prepare budget to be adopted by Council of Ministers (first week of June)</li> <li>▪ Ministers, directors of independent state institutions and municipal/provincial governors provide details on their revenue and expenditure and send to MEF</li> <li>▪ Discussion with ministers, directors of independent state institutions and municipal/provincial governors on their proposals (August)</li> <li>▪ Finalize balance of revenue and expenditure (September)</li> </ul>
<b>October – December</b>	<ul style="list-style-type: none"> <li>▪ Draft law for the management of the year is submitted to Council of Ministers (first week of October)</li> <li>▪ Submit draft law to National Assembly (first week of November)</li> <li>▪ Submit draft law to Senate (first week of December)</li> </ul>
<b>Source:</b> <i>National Budget Law (RGC, 2007).</i>	

In November, the National Assembly discusses, debates, proposes amendments if necessary and finally adopts the budget before sending it to the Senate. Following approval by the National Assembly, the adopted or amended draft Budget Law is sent to the Senate for examination and recommendations. In the first week of December, the budget is submitted to the Senate. If the Senate gives its approval, the draft Budget Law is sent directly to the King for promulgation. However, if the Senate calls for modifications, the draft Budget Law is sent back to the National Assembly. The National Assembly then examines and decides to accept or reject all or

some of the provisions or any terms that the Senate calls for. The process of sending back and forth the draft Budget Law between the National Assembly and the Senate cannot exceed 10 days. After adoption of the law by the National Assembly and the Senate, the King signs and promulgates the adopted Budget Law.

The calendar for budget preparation is very clear. On principle, if the law cannot be passed, that for the management of the previous year is applicable. This means that the new calendar does not propose a specific timeframe for ministers to revise the draft law in case of a negative vote by the National Assembly.

### 3.4 Implementation, Monitoring and Control (January 1 to December 31)

After the National Budget is adopted as law, the government starts implementation. Usually, all ministries and independent government institutions can start spending the money from January of each year. There are different ways of getting the cash disbursed for expenditures, depending on type. In general, expenditures in the ministry are grouped into three categories:

- **Payroll** (staff salaries, pension funds and other expenditures related to staff). For this category of expenditure, the ministry submits a proposal to the Civil Service Secretariat for review before sending it to MEF for approval. After it is approved, the document is sent to the National Bank of Cambodia (NBC) for check issuance.
- **Operating costs:** The budget proposal is submitted by the line ministry directly to MEF for checking and approval. Then the NBC issues a check for money disbursement.
- **Direct expenditure:** For this type of expenditure, the money is paid directly to the supplier of goods or services. This usually occurs through a bidding process, carried out by the line ministry based on MEF guidelines and procedures. The result of the bidding is submitted to MEF for approval. As with other types of expenditure, after it is approved, the document is sent to the NBC for money disbursement.

After money is disbursed based on the procedures above, the line ministry/implementing agency will implement the activity, following MEF financial guidelines.

The MEF Department of Budget and Finance, the MEF Department of General Inspectorate and the internal audit department within each public institution exercise internal control over public spending during implementation; line ministries and other independent state institutions are the actual implementers of the National Budget.



- The Department of Budget and Finance distributes budgets to all ministries and to other government institutions for implementation; it also monitors execution of revenues and expenditures according to the budget allocated to ministries, institutions and provinces/communes.
- The Department of General Inspectorate conducts general inspections of ministries and government institutions on expenditure operations and the accountability of public funds administrators. It also conducts inspections of all financial operations of public institutions and state enterprises, etc. It conducts investigation of claims and complaints made by citizens in connection with economic management, and can file complaints to the court.
- The internal audit department within each institution, ministry and public enterprise independently examines and evaluates the effectiveness of the internal control system. These departments ensure that reliable financial reporting is carried out effectively, and that operations are in compliance with applicable laws, regulations, policies and procedures, etc.

### 3.5 Budget Auditing

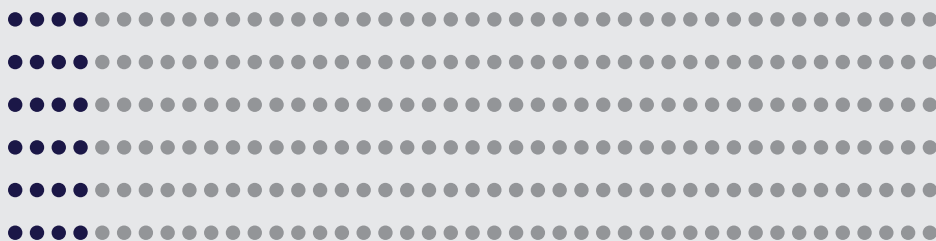
The National Audit Authority (NAA), an independent public entity, is responsible for executing the external audit function of the government. The Auditor-General is empowered to conduct audits on accounting records, accounts, management systems, operation controls and programs of government institutions in accordance with generally accepted auditing standards and the government's auditing standards<sup>5</sup>. The external audit includes the implementation of the following types of audits:

- Audit on financial statements;
- Audit on the management of credit projects financed by external sources;
- Audit on management systems and operations of all institutions;
- Audit on evaluation, efficiency and effectiveness of operations.

The audit process is guided by the Law on Audit of the Kingdom of Cambodia. According to the law, the government is obliged to provide documents of settlement of the annual budget to the National Assembly and the Senate for examination and approval. These reports also need to be submitted to the NAA for auditing within nine months of the close of the financial year. The NAA prepares an

<sup>5</sup> Article 1 of the Law on Audit of the Kingdom of Cambodia, March 3, 2000.

auditing report and submits this to the National Assembly and the Senate. The National Assembly concludes the auditing process by means of passing the budget settlement law. In this way, conclusions are drawn concerning good or unsatisfactory budgetary implementation.



## 4 TRENDS IN THE CAMBODIAN BUDGET

To guide the use of resources, the RGC has developed the NSDP, which covers a five-year period. The current NSDP is for the period from 2006 to 2010. It is to be implemented through the National Budget and the Public Investment Program, which is expected to guide the RGC's development efforts. The NSDP has been characterized by the Prime Minister as 'the blue print for further progress' and 'the single all-encompassing document for the next five years'. It is known as the strategy to achieve the Cambodian Millennium Development Goals (CMDGs), in which key socioeconomic policy priorities are: eradication of extreme poverty and hunger, universal nine-year basic education, increased gender equality and the reduction of child mortality. Many new policies and plans have been set out in order to achieve these goals. However, to be meaningful, the new policies and sector-level plans have to be linked to the budget, the most important instrument of the RGC in translating its policies into action. Box 4.1 describes some of the difficulties faced by the National Assembly and MEF when making decisions on public spending.

### **Box 4.1: Difficulties Faced by the RGC in Expenditure Allocation**

The process of formulating the budget to translate policies into action and to meet desired outcomes and goals is complex, and requires complex analysis. With limited resources, the RGC needs to choose between investment in government administration, economic sectors, (agriculture, transport, public works and rural development) and social sectors (education, health, social protection and other social services).

As pointed out by the World Bank (2007), making recommendations as to what is the optimal allocation for government spending is difficult. One reason for this is that increases in capital expenditure (building a road/school/hospital) can only be done properly if government has enough staff to implement the project, which means that additional recurrent expenditure (wages/operational costs) may be necessary. Therefore, it is not immediately clear whether capital expenditure has to be preferred over current expenditure. Another issue is that spending on infrastructure is complementary to social expenditure. As such, in order to improve enrolment rates in a particular district, it is possible that a rural road may do more than building another school. Consequently, it is also not immediately clear

what sectors need to receive priority to achieve a certain social objective.

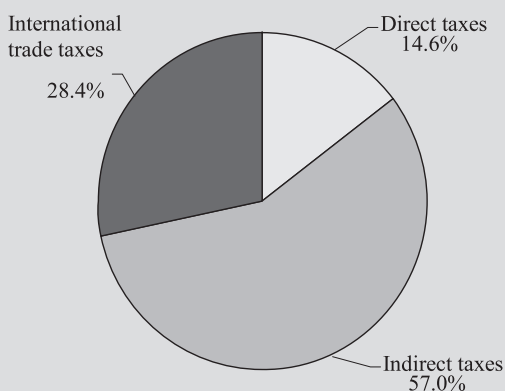
Despite these difficulties, government and the National Assembly need to make decisions on allocations every year. In order to make the best possible decisions, both government and the National Assembly should have as much information as possible. Therefore, it makes good economic sense to listen closely to citizens' needs, through consultation with the population and engagement with civil society organizations.

#### 4.1 Trends in Revenue

The domestic revenue side of the budget is composed of current revenues and capital revenues (see Section 2.3). For several years, domestic capital revenues have been minimal. From 2000 to 2004, capital revenues contributed less than 2 percent to total domestic revenues; the rest was contributed by current revenues. Sources of domestic capital have included privatization, sale of immovable properties (e.g. privatization of rubber plantations and sale of public land – in the 2007 Budget Law, these revenues are classified as current revenues) and domestic borrowing. The share of capital revenues jumped to 5.8 percent in 2005, owing largely to an increase in revenues from privatization (from CR9 billion (US\$2.2 million) in 2004 to CR133.6 billion (US\$32.1 million). In 2006, capital revenues continued to increase, to 11.6 percent of total domestic revenue, as a result of unexpected gains from the Multilateral Debt Relief Initiative (MDRI)<sup>6</sup>.

However, these increases cannot be considered a significant change to the trend in

**Figure 4.1: Share of Tax Revenue in 2006**



**Source:** *Compiled from MEF 2006 budget implementation.*

<sup>6</sup> In January 2006, under the MDRI, the IMF erased the outstanding owed to the fund, valued at US\$82 million.

revenue collection. By definition, increases in capital revenue are unstable, and vary significantly from year to year. Furthermore, most of the time, capital revenues are a one-time deal.

The current revenue for 2006 was at CR2,881.7 billion (US\$701.7 million), reaching 9.8 percent of GDP. This showed an increase of 16.5 percent compared with 2005. Revenue from tax was the main source of current revenue; this represented 78.8 percent of total current revenue in 2006, equal to 7.7 percent of GDP.

The government collects three different types of taxes:

1. Direct taxes, which are paid directly to the government, include payroll taxes, profit taxes and land and property taxes. Direct taxes collected in 2006 were worth CR331 billion (US\$80.5 million), 162 percent of the budget plan. This had increased at an impressive rate of 49 percent compared with the preceding year.
2. Indirect taxes have been a major source of tax revenues for several years. These accounted for 57 percent of tax revenues in 2006 – 16 percent more than in 2005 – and 4.4 percent of GDP. Indirect taxes are paid to a second party, who then passes them on to government. They include turnover tax, VAT and excise duties on goods and services, such as import tariff on fuel, excise on alcohol and cigarettes, etc. VAT alone accounted for 66.1 percent of total indirect taxes in 2006.
3. International trade taxes are composed of import and export duties and taxes. In 2006, the government collected CR644.4 billion (US\$80.5 million) in international trade taxes, 12.5 percent more than in 2005. However, its share of GDP dropped slightly, from 2.2 percent to 2.1 percent, owing to rapid GDP growth (at 10.8 percent at 2000 constant prices).

Non-tax revenue consists of revenues from fisheries, forestry, royalties, post and telecommunications, visa fees, profits from banking, etc. In 2006, non-tax revenue amounted to CR610.9 billion (US\$148.7 million), 8.6 percent more than in 2005, and represented 2.1 percent of GDP. Five major sources of non-tax revenue in 2006 were visa fees (CR95.3 billion/US\$23.2 million), quota auctions and export licenses (CR88.4 billion/US\$21.5 million), post and telecommunications (CR83 billion/US\$20.2 million), casinos (CR77 billion/US\$18.7 million) and tourism (CR59.2 billion/US\$14.4 million).

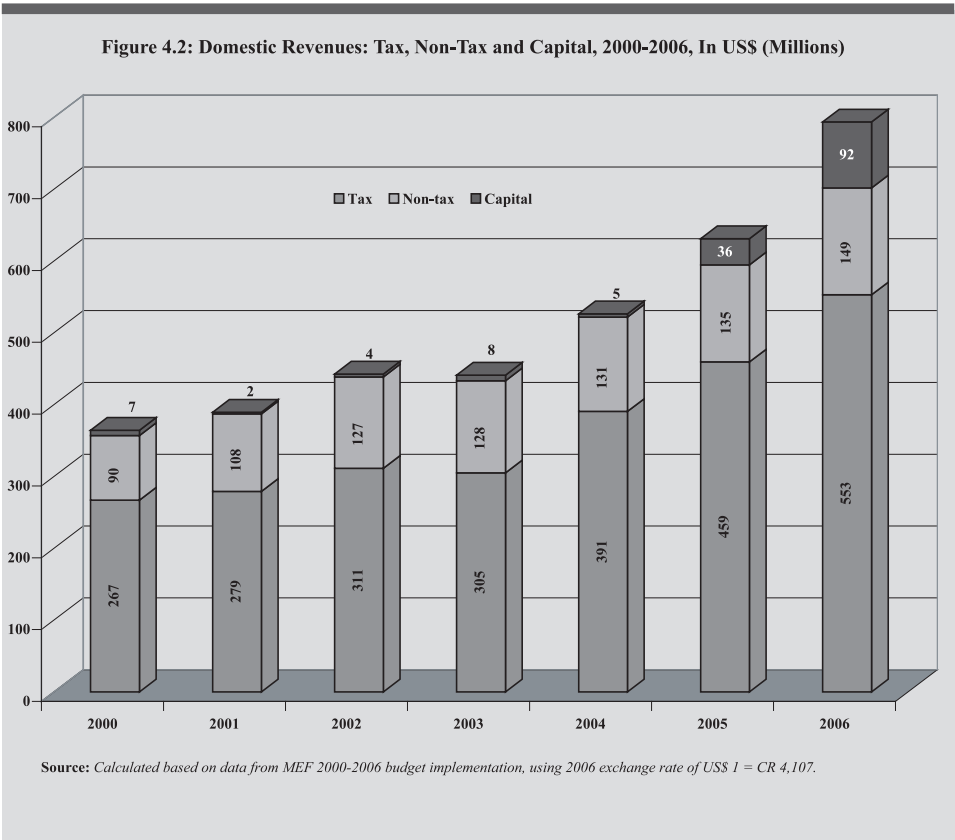
Similar to tax revenues, non-tax revenues have increased every year since 2000. In 2000, non-tax revenue represented 25.2 percent of total domestic revenue; this rose to 29.6 percent in 2003, but dropped to 21.2 percent in 2006.

In general, recent years have shown a great deal of progress in domestic current revenue collection. The amount of revenue has grown substantially. In real terms,

revenues collected in 2004 indicated a 22 percent increase compared with 2003. This increase continued at 17 percent and 14 percent in 2005 and 2006, respectively. However, when compared with GDP, this trend does not show significant improvement. The current revenue-to-GDP ratio has remained almost the same, fluctuating around 9.5 and 10 percent, since 2000. In addition to being a result of governance problems, this owes mainly to rapid growth in economic activities, including informal agriculture and garment industry, which are largely tax-exempt.

It is important to note that off-budget revenues are significant (World Bank and IMF, 2005). These are mainly non-tax revenues collected by line ministries or institutions and used to finance their own institution. Capturing all these off-budget revenues will surely increase current revenue-to-GDP ratios, as well as increasing transparency. Incorporating off-budget revenues into the budget is seen in the action plan of the PFMRP. However, so far, progress has been slow, owing to lack of cooperation from line ministries.

By 2009, the government aims to improve revenue collection to reach 12.5 percent of GDP.



## 4.2 Trends in Expenditure

As mentioned earlier, allocations should be guided by the NSDP, which aims ‘to reduce poverty rapidly, and to achieve other CMDGs and socioeconomic development goals for the benefit of all Cambodians’. In order to achieve the stated objectives, government expenditure should be pro-poor, meaning that it should aim to reduce poverty. Although exact definitions as to what expenditures in the budget are pro-poor are not available, there is a general consensus that expenditures that seek to stimulate small-scale agriculture, promote basic healthcare, support primary and secondary education, improve access to drinking water and improve sanitation fall into this category.

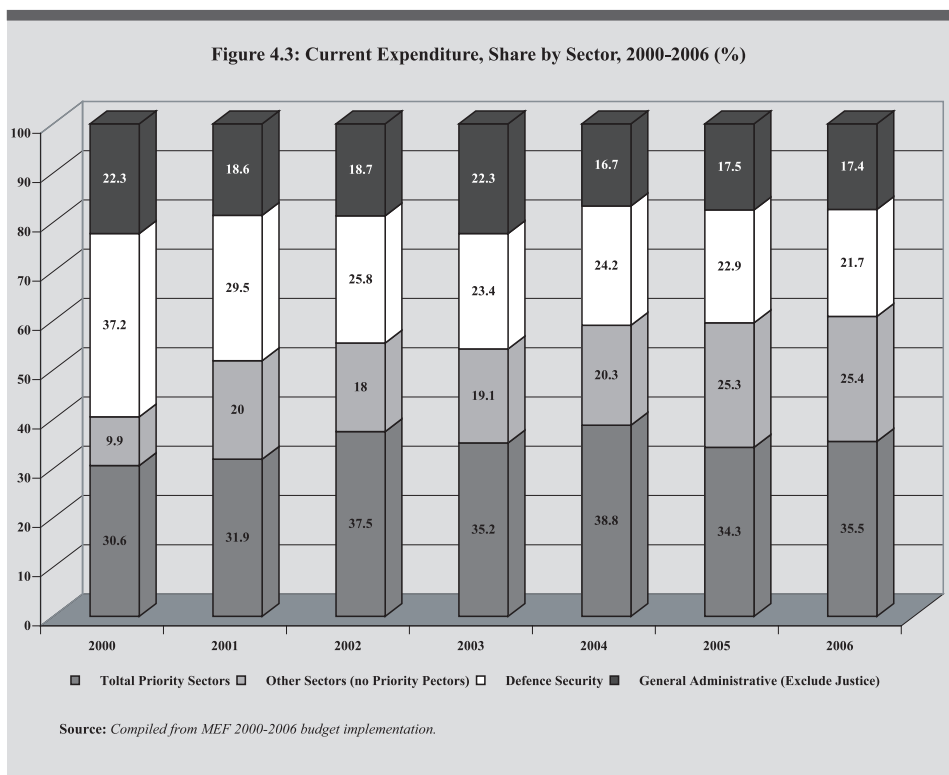
In order to operationalize the pro-poor concept, the RGC has identified seven ministries as priority: i) Ministry of Education, Youth and Sports; ii) Ministry of Health; iii) Ministry of Women’s Affairs; iv) Ministry of Agriculture, Forestry and Fishery; v) Ministry of Rural Development; vi) Ministry of Land Management, Urban Planning and Construction; and vii) Ministry of Justice. Granting these ministries the label of ‘priority’ raises the expectation that their budgets will be given precedence over ‘non-priority’ areas. For instance, it is reasonable to expect that budgets of priority ministries will receive first priority in case there is additional money available from the National Budget.

The analysis presented below provides an overview of trends in government budgets, compares allocations to priority sectors versus non-priority sectors, and describes trends in allocations to individual priority sectors. However, it needs to be noted here that an attempt to analyze the overall trend of government expenditure (both current and capital) in different sectors is difficult, owing to lack of data on budget implementation in capital expenditure. The reason for this is that there are two sources of funding for capital expenditure: domestically financed public investment (implemented within the budget) and direct externally financed public investment (implemented directly by donors and, therefore, off-budget). The proportion of direct external financing in the total capital budget is very high. In the Budget Law, this represented 75.2 percent of total capital expenditure in 2004, and 72.9 percent in 2006. These major shares of capital spending are operated outside the National Treasury. Currently, given the nature of this implementation, even MEF itself has very limited data on this category. The problems associated with this large amount of off-budget expenditure will be the subject of future work of the Budget Project at the NGO Forum on Cambodia.

### 4.2.1 Current Expenditure (implemented budget)

Figure 4.3 below provides an overview of the actual current expenditure from

2000 to 2006 in four broad categories: General Administration, Defense & Security, Priority Sectors, Other Sectors<sup>7</sup> (non-priority). The figure shows that current expenditure on Defense & Security as a share of total current expenditure dropped significantly, from 37.2 percent to 21.9 percent. Current spending on General Administration (excluding Justice) decreased from 22.3 percent to 17.4 percent as a share of total current expenditure. The share of the seven priority sectors increased from 30.6 percent to 35.3 percent over the same period. However, at the same time, current spending on all Other Sectors (non-priority) increased at an even faster rate from 9.9 percent in 2000 to 25.4 percent in 2006.



As shown in the table in annex 4, Government current expenditure in 2006 amounted to CR1,937,583.7 million (US\$471.7 million), which is a 65 percent increase relative to 2000. As shown in the same table, spending on key social sectors expanded by 90 percent during the same period, however the priority ministries did not benefit from this equally, which can also be clearly seen in table 4.1 below.

Real current expenditure on **Education** increased by 90 percent between 2000 and 2006. As a share of total current expenditure, it increased by 4 percentage point,

<sup>7</sup>The category of Other Sectors (non-priority) contains the following: Culture and Fine-Arts; Environment; Information; The category of Other Sectors (non-priority) consists of: Labor and Vocational Training; Public Worship and Religion; Social Affairs, Labor & Vocational Training; Civil Aviation Secretariat; Commerce; Industry, Mines and Energy; Posts and Telecommunications; Public Works and Transport; Tourism; Water Resource and Meteorology; and all items grouped under the heading Miscellaneous.



from 14.8 percent to 18.8 percent over this period.

Current expenditure in **Health** expanded by 109 percent between 2000 and 2006, while its share in total current expenditure increased from 7.9 percent in 2000 to 11.3 percent in 2006. As an amount, it grew more than twofold, from CR92,828 million (US\$23.8 million) in 2000 to CR219,123.3 million (US\$53.3 million) in 2006. Further it is worth noting that in 2006, health and education combined accounted for 85 percent of all current expenditure in the seven priority sectors.

Current spending on **Agriculture, Forestry & Fishery** doubled between 2000 and 2006 and amounted to CR45,831.8 million (US\$11.1 million) in 2006, expressed in 2000 constant prices. In 2006, current spending in Agriculture, Forestry & Fishery represented 6.7 percent of current expenditure in the priority sector.

In 2006, current spending on **Rural Development** amounted to CR24,235.1 million (US\$5.9 million) which is an increase of 228 percent compared to 2000. Its share of total current expenditure on priority sectors was 1.3 percent in 2006.

Current expenditure on **Justice** has increased by 90 percent between 2000 and 2006. Expressed in constant 2000 prices, it was CR5,688.00 million (US\$1.4 million) in 2000 and reached CR10,786.9 million (US\$2.6 million) in 2006. However, as a share of total current priority expenditure, it represents only 1.6 percent.

Between 2000 and 2006, current spending on **Urbanization & Construction** grew

**Table 4.1: Current Expenditure 2000-2006 as a Share of Total Current Expenditure (%)**

	2000	2001	2002	2003	2004	2005	2006
<b>Total expend. by ministry</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>
<b>Gen. Admin. (excl Justice)</b>	22.3	18.6	18.7	22.3	16.7	17.5	17.4
<b>Defense &amp; Security</b>	37.2	29.5	25.8	23.4	24.2	22.9	21.9
<b>Other sectors</b>	9.9	20.0	18.0	19.1	20.3	25.3	25.4
<b>Total priority sectors</b>	<b>30.6</b>	<b>31.9</b>	<b>37.5</b>	<b>35.2</b>	<b>38.8</b>	<b>34.3</b>	<b>35.3</b>
Education	14.8	14.8	18.4	17.1	18.7	17.8	18.8
Public Health	7.9	9.2	10.4	9.8	11.0	11.4	11.3
Women's Affairs	4.5	4.2	4.1	4.1	4.9	0.5	0.6
Agriculture	1.9	2.2	2.5	2.2	2.2	2.4	2.4
Rural Development	0.6	0.9	1.2	1.0	1.0	1.1	1.3
Justice	0.5	0.4	0.5	0.6	0.6	0.6	0.6
Urbanization & Construction	0.4	0.3	0.4	0.4	0.4	0.4	0.5

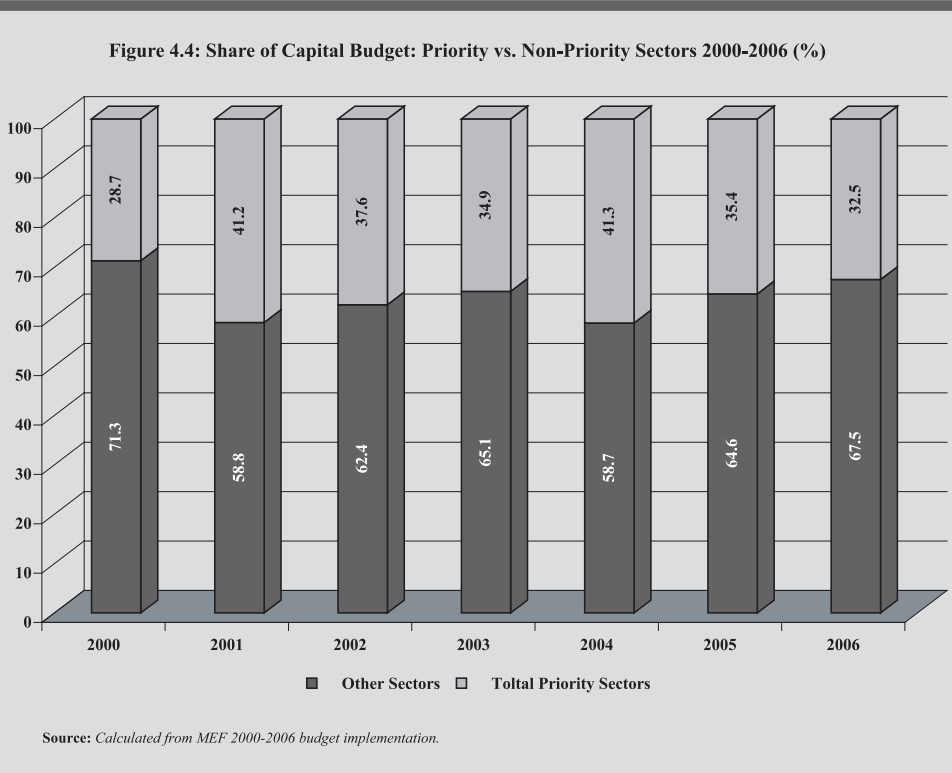
**Source:** Calculated from MEF 2000-2006 budget implementation.

by 144 percent. Its current spending increased from CR4,252 million (US\$1.1 million) in 2000 to CR10,369.8 million (US\$2.5 million) in 2006. As a share of total current priority expenditure, it represents only 1.5 percent.

It is surprising to see a negative trend in **Women’s Affairs** current spending. Between 2000 and 2006, Women’s Affairs current spending was severely cut, by 80 percent. It was CR52,879 million (US\$13.5) in 2000 but only CR10,703.7 million (US\$2.6 million) in 2006 representing 1.6 percent of total current priority expenditure.

### 4.2.2 Capital Expenditure (Budget Law)

Capital expenditure is generally viewed as a main driver of development. There are two sources of funding for capital expenditure: external financing and domestic financing. External financing has been the main source, representing 75.2 percent of total capital expenditure in 2004 and 72.9 percent in 2006. However, as mentioned earlier, at the level of ministries, we only have access to data on domestically financed capital expenditure, and only from 2004 onward. As a result, we will analyze the trend of capital expenditure based on the Budget Law and not on budget implementation (as in the current expenditure section, where data on budget implementation are available).



Increasing capital expenditure with an emphasis on priority sectors is the aim of the RGC's pro-poor fiscal policy. Although there is an increase over the whole 2000-2006 period, a negative trend can be seen in Table 4.2 below where the share of the capital budget for priority sectors has been decreasing since 2001, with an exception in 2004.

The data in Table 4.2 below and annex 4 show clearly that there is no consistent trend in budgeted capital expenditure in the priority sectors, although an increase can be observed over the 2000-2006 period. For instance, the priority sectors were allocated less money in both terms – total amount and as a share of total capital expenditure – from 2001 to 2006. In 2001, the capital budget for priority sectors was CR797,352 million (US\$202.8), but this dropped to only CR476,131 million (US\$116 million) in 2006. Regarding total capital budget, it dropped by nearly 10 percentage point over this period, from 41.2 percent to only 32.5 percent.

**Table 4.2: Budget Law Capital Expenditure 2000-2006, Share of Total Capital Budget (%)**

	2000	2001	2002	2003	2004	2005	2006
<b>Total capital budget</b>	100	100	100	100	100	100	100
<b>Other sectors</b>	71.3	58.8	62.4	65.1	58.7	64.6	67.5
<b>Total priority sectors</b>	28.7	41.2	37.6	34.9	41.3	35.4	32.5
Education	9.9	7.9	6.0	8.4	9.6	11.9	8.2
Public Health	19.9	23.2	20.8	20.2	23.2	19.5	18.8
Women's Affairs	1.8	1.4	1.3	1.7	4.1	2.9	3.4
Agriculture	0.9	6.7	9.6	8.4	9.9	8.0	6.0
Rural Development	4.9	9.1	5.1	3.7	3.2	3.7	3.5
Justice	0.8	0.4	0.4	0.2	0.2	0.5	0.2
Urbanization & Construction	0.4	0.4	0.3	0.6	0.7	0.8	0.7

**Source:** Calculated from MEF 2000-2006 budget implementation.

#### 4.3 Trends in Interest Payment and Debt Amortization

The trend in payment on interest and debt amortization is quite alarming. As illustrated in Table 4.3, the payment on interest increased by more than double in real value, from CR20 billion (US\$5.1 million) in 2000 to CR40.8 billion (US\$9.9 million)

in 2006. Debt amortization began in 2001 with CR4 billion (US\$1 million). It grew more than 10 times to CR45 billion (US\$11 million) in 2006, accounting for 14.5 percent of total domestically financed capital expenditure. Given the current situation, where the volume of loans from both bilateral and multilateral development partners keeps growing, this trend is likely to continue for years to come. This should be seen as a concern for future government allocation of resources, since payment of interest and debt amortization is the obligation of the government, and other spending can only be allocated after this obligation is fulfilled. This means that rising interest payments and debt amortization will restrict ability to meet other development spending needs. However, in its debt analysis, the IMF<sup>7</sup> concluded that Cambodia's debt is still sustainable (see Section 4.5 for more detail).

**Table 4.3: Trend in Debt Amortization and Interest Payments, 2000-2006**

Year	2000	2001	2002	2003	2004	2005	2006
Capital expenditure	887.0	1073.1	1342.8	1112.8	1081.7	1134.2	1146.4
Locally financed	309.0	275.8	327.0	316.5	268.4	269.5	311.0
Foreign financed	578.0	797.3	1015.8	795.4	812.4	864.7	835.4
Debt amortization		3.9	7.7	56.1	22.7	32.2	45.0
<i>Debt/domestic financed capital exp.</i>	<i>0.0%</i>	<i>1.4%</i>	<i>2.4%</i>	<i>17.7%</i>	<i>8.4%</i>	<i>11.9%</i>	<i>14.5%</i>
Current expenditure	1,177	1380.1	1523.7	1670.7	1582.2	1681.3	1931.9
Interest payment	20.0	21.4	27.1	32.3	44.4	47.2	40.8
<i>Interest payment/total current exp.</i>	<i>1.7%</i>	<i>1.6%</i>	<i>1.8%</i>	<i>1.9%</i>	<i>2.8%</i>	<i>2.8%</i>	<i>2.1%</i>

**Note:** Value in CR billions, at 2000 constant prices.

**Source:** Calculated from MEF 2000-2006 budget implementation

#### 4.4 Decentralization and the Budget

Decentralization and deconcentration (D&D) has been viewed as an important tool for pushing towards democratic government, in addition to promoting good governance and improving service delivery. The adoption of legislation in 2001 to replace appointed local authorities with directly elected commune councils established a mechanism for the direct participation of citizens in local governance and reinforced the principle of downwards accountability of government to citizens. Com-

mune council elections in 2002 and 2007, and the gradual development of council capacity, underscore the emergence of viable structures of sub-national governance. However, managerial and financial empowerment of local authorities still has much space for improvement towards a sustainable democratic governance system.

Article 146 of the Constitution provides a legal basis for sub-national administration, with the provision for the adoption of an organic law, which still remains to be completed. The organic law is expected to delineate more clearly the roles and relationships of the province, district and commune, to differentiate between rural and urban governance structures, and to provide a legal basis for the allocation of functions and revenue to sub-national units. Besides this, several other important issues still need to be addressed adequately: the improvement of transparency and accountability within local administrative mechanisms, the human resources of local administrations, commune revenue collection capacities and popular participation in local decision making, as well as in local development.

Currently, decentralization is implemented at commune level, supported by a wide range of laws and regulations, such as the Law on the Administration and Management of Communes and the Law on the Election of Commune Councils. In addition to political empowerment, the commune council is also provided with limited decision-making authority on service delivery and some fiscal matters. The commune is legally entitled to three main sources of revenue: own-source revenues, funds transferred from central government and local contributions. Up to the present, legislation defining the powers of communes to generate own-source revenues has not been adopted, and the commune budget has remained largely dependent on funds transferred from central government. The average amount transferred from central government to each commune was CR48 million (US\$11,700) in 2006 (Sieng, 2006: 12). In 2007, direct financing of commune councils through the Commune Sangkat Fund amounted to approximately 2.6% of the budget. Without practical policies, communes are still unlikely to generate much revenue, as they can be subject to the will of their superiors, the district and provincial authorities.

Commune capacity to carry out fiscal duties is also a concern. With limited human resources capacity and economic potential in the community, only a small percentage of communes are confident to stand alone, without support from central government. A clear fiscal framework, technical assistance and capacity building for commune staff are crucial for the system to be operational.

#### 4.5 Public Debt

The Cambodian economy has been enjoying double-digit growth in recent years. However, government-collected revenue remained low compared with its spending, causing a large budget deficit every year. As a result, the budget remained heavily re-

liant on external financing in both grants and loans, increasing the country's debt.

According to the IMF (2006), Cambodia's national debt has already reached US\$3,391 million (CR13,926.8 billion). External debt represented US\$3,182 million (CR13,068.4 billion), or 94 percent, and domestic debt was US\$210 million (CR862.4 billion). This amount of debt is already equal to 54 percent of GDP.

**Table 4.4: Public Debt Outstanding,  
2005, in US\$ (millions)**

<b>External debt</b>	<b>3,180</b>
Multilaterals	1,149
<i>IMF</i>	81
<i>IDA</i>	461
<i>ADB</i>	568
Bilateral	2,031
<i>Russia</i>	1,525
<i>United States</i>	302
<b>Domestic debt</b>	<b>210</b>
<b>Total</b>	<b>3,391</b>

**Source:** IMF 2006.

Around 34 percent of external debt is owed to the multilateral creditors, namely the Asian Development Bank (ADB), the IMF and the World Bank. The US and the Russian Federation are the two largest creditors, covering around 64 percent of the total Cambodian external debt. Currently, the RGC is not servicing its debt, and has been in negotiations with these two nations through the Paris Club Framework Agreement to restructure the debt. Negotiations with the US have been mainly about the amount of principle. The two parties have now reached agreement on the total amount of principal due, at US\$162 million (CR665.3 billion). With the Russian Federation, negotiations have dealt with the exchange rate between the Russian ruble and the US dollar. So far, Russia has agreed to reduce 70 percent of the debt, from US\$1.52 billion (CR6,242.6 billion) to US\$457 million (CR1,876.9 billion). With this result, as IMF (2007) tells us, the total Cambodian external public debt was reduced to US\$2.25 billion (CR9,258.7 billion) or 31 percent of GDP. This ratio is projected to decline further in 2007.

Based on analysis, the IMF and the International Development Association (IDA) of the World Bank (2007) concluded that Cambodia's debt situation remained on a sustainable path. In its 2006 Article IV Report, the IMF concluded that Cambodia's

debt was at high risk of distress. Risk was reduced to moderate this year, owing to higher-than-expected GDP growth and continued large-scale concessional financing from both traditional and new development partners, used to justify reduction of risk of debt distress.

Recently, Cambodia received a B+ sovereign credit rating by Standard and Poor's and a B2 from Moody's. According to the 2007 IMF Staff Report, this could provide an opportunity for commercial borrowing. However, the IMF also warns that debt sustainability would be at greater risk if the RGC borrowed at commercial terms.

As indicated, the RGC is not yet servicing its debt to the two major creditors. However, if we look at budget implementation, we can see that external debt amortization began in 2001, and has been growing at a very fast pace. Debt amortization increased nearly 13-fold, from CR4 billion (US\$1 million) in 2001 to CR55.2 billion (US\$13.4 million) in 2006; interest payments also rose over this period, from CR22 billion (US\$5.6 million) to CR50 billion (US\$12.1 million).







## 5 PERTINENT ISSUES

### 5.1 Access to Information on the Budget

Access to information on the National Budget is crucial for the development of Cambodia as a democratic country. With better access to budgetary information, citizens will be able to participate more, for instance in monitoring budget implementation, and thus hold the government accountable and enhance government effort in promoting economic growth, social development and good governance.

The RGC has recognized the essential character of access to budget information and has made a commitment to improving availability of budget information. Under the PFM RP, monthly up-to-date reports on the progress of budget implementation, including a comprehensive mid-year review, have to be publicized. In addition, the program indicates that reports from the NAA will be disclosed to the public.

However, the PFM RP does not provide a clear timeframe as to when these commitments will be achieved. Currently, access to information and communication is still limited, as is the level of detail provided on the National Budget. The RGC produces and documents various kinds of budget-related information, but not all of this is available to the public. Documents that contain budget information and are known to be publicly available are the National Budget Law and the Budget Settlement Law. These two documents only became public after they were promulgated by the King. Below we see a description of the different budget-related documents that are publicly available, who is involved in the production, and where they can be obtained<sup>8</sup>.

#### 5.1.1 Budget Documents that are Publicly Available

The **National Budget Law** is the most important document containing budget information released to the public. In Cambodia, the National Budget Law is prepared for the state's financial management in the coming year. In addition to figures showing the amount planned for revenue mobilization and budget expenditure al-

<sup>8</sup> All publicly available documents can be collected from the Budget Project at the NGO Forum on Cambodia.

located for each sector, the law also contains explanatory notes, the drafting context and any amendment or new article of the Financial Law of 1993.

The Budget Law is prepared by MEF, approved by the Council of Ministers, passed by the National Assembly, adopted by the Senate and promulgated by the King. Once it has been promulgated (towards the end of December each year), it becomes a public document and is available at i) the National Library; ii) the Senate Library; and iii) the National Assembly Library.

**Budget management documents** are prepared by MEF for the purpose of state budget management. MEF publishes four types of budget document:

- **Budget Management:** In addition to the Budget Law, this document provides a macroeconomic overview and various guidelines and procedures for budget implementation.
- **State Budget for Management of the ‘Central Government’:** provides a detailed plan for revenue mobilization and expenditure separately for each ministry, government authority and institution of the central government.
- **State Budget for Management of ‘Line Departments and Institutions at Provincial/Municipal Level’:** Detailed information on revenue and expenditure of provincial line departments of each ministry/authority is presented in this document.
- **Province and Municipality Budget for Management:** This document provides information on budgeted revenues and expenditures for each province. It also contains the MEF Prakas (Ministerial Order), in which each person/department responsible for implementing the budget is identified.

Within MEF, the Department of Budget can provide copies of the budget management documents about three months after the promulgation of the law. These documents should be available at the Department of Budget in March/April.

**The Monthly Bulletin of Statistics** is published by MEF. This aims to disseminate to the public statistical information on various economic areas, and includes the Table of State Financial Operations (TOFE), describing actual implementation of capital and current revenues and expenditures of the state. However, data are aggregated and there is no breakdown by ministry available.

The Monthly Bulletin of Statistics is produced by MEF two weeks after the reporting period has ended and should be on the website soon after that. The Bulletin can be found at <http://www.mef.gov.kh> in the ‘publications’ section.

**The Budget Settlement Law** describes actual revenues generated and real expenditure in the previous fiscal year in comparison with the original proposals. However, the law does not explain the enacted level and the actual outcomes of the

expenditure and how the money is spent. The Budget Settlement Law is prepared by MEF, approved by the Council of Ministers, passed by the National Assembly, adopted by the Senate and promulgated by the King.

Now, in 2007, the latest Budget Settlement Law publicly available is from 2004. Once the Budget Settlement Law has been promulgated (April 24, 2004 in this case), it becomes a public document and is available at i) the National Library; ii) the Senate Library; and iii) the National Assembly Library.

### *5.1.2 Budget Documents that are not Publicly Available*

A number of budget-related documents in Cambodia are produced but not made publicly available. These documents include:

The **First Budget Circular** gives macroeconomic aggregates that provide revenue projections and estimates of resources available for the forthcoming year. This is produced by MEF in May/June.

**Monthly figures on budget implementation** provide detailed information on state revenues and expenditure by ministry/institution, by MEF.

The **mid-year review** provides an overview of the differences between planned and actual expenditures during the year and should include remedial action if the implementation plan is threatened, for example, by revenue flows underperforming or the arising of an unexpected need for additional expenditure. The mid-year review is carried out by MEF in July.

**National audit reports** are produced by the NAA every year, but only submitted to the National Assembly and the government. The report is perceived as secret and not suitable for public disclosure.

## 5.2 Emerging Sources of Revenue

The recent exploration of oil and gas in Cambodia's territorial sea and indications of abundant mineral resources in the eastern and northern parts of the country make it highly likely that Cambodia will turn into a small oil-producing and mining country, raising a substantial amount of its revenues from these extractive industries.

### *5.2.1 Oil and Gas*

At the time of writing, estimates of the amount of oil that could be commercially

exploited are unclear, as are estimates of the timing and size of expected revenues for the RGC. It is certain, however, that inflows will be substantial compared with the current (2007) National Budget Law and the latest scenario provided in the 2007 IMF Staff Report, which states that the RGC may receive an income of up to US\$1.7 billion in 2021, increasing from US\$174 million in 2011. From these figures, it is clear that there will be a substantial impact, given that government revenue in 2006 amounted to almost US\$710 million.

These revenues should also come from the companies that currently have exploration licenses for the six offshore blocks. Of these companies, the consortium led by Chevron is at the most advanced stage, and is expected to make an announcement on the amount of recoverable oil in Block A towards the end of 2007. Other consortia that have been granted exploration licenses by the Cambodian National Petroleum Authority include the following consortia leaders: MEDCO (Indonesia), Petrotech (China), Singapore Petroleum Company, PTTEP (Thailand), Polytech (China) and CNOOC (China). Besides these six undisputed offshore blocks, the four blocks in the Overlapping Claims Area between Thailand and Cambodia are expected to generate even more revenues once negotiations have paved the way for exploration and exploitation by different oil companies. Further revenues are expected from some of the potential onshore sites in Cambodia, however there is currently little information available concerning locations and companies involved.

### *5.2.2 Mining*

In addition to oil and gas, Cambodia has huge reserves of minerals and ore, which can be exploited in the near future. It has been seen that there are about 2.5-4.8 million tons of iron ore in the northern part of the country, and another 5.2 million tons in Kampong Thom province. Moreover, there are about 120,000 tons of manganese ore in Kampong Thom alone<sup>9</sup>. Besides this, the northeastern part of Cambodia, particularly Mondolkiri and Ratanakiri provinces, are believed to have significant reserves of gold, copper and bauxite. At present at least 6 international companies have large area exploration licenses, all at different stages of exploration. BHP Billiton, with its one hundred thousand hectare bauxite concession, expects to reveal its initial exploration findings by mid-2008.

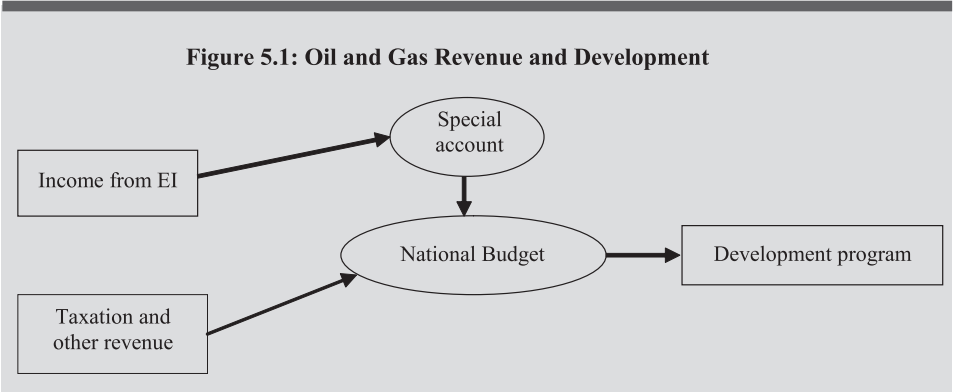
In similar ways to oil and gas, mineral exploitation will generate large amounts of revenue for the RGC through royalties and taxes. Yet, it is not possible to estimate at this stage how much revenue the RGC will receive. However, many predict that revenue from mining will be substantial, and likely to last for a longer period of time (30 years +) than oil (~ 15 years).

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<sup>9</sup> <http://www.photius.com>.

5.2.3 Implications of Revenues from Extractive Industries

From these estimates and assumptions, prospective government revenue from the so-called Extractive Industries (EIs) is significant, and could represent a major new source of revenue for the state which, if properly managed, could assist the government greatly with developing the country effectively. Figure 5.1 shows income generated by EIs, which will be a new source of government revenue – the supply side of the National Budget. The development program, which should have a direct impact on people’s livelihood, particularly the poor, and the economy, can be seen as the demand side. The way to ensure that EI revenue has an impact on the poor is in the use of the National Budget. Therefore, if this potentially huge government budget is spent appropriately, to respond to the most needy sectors and public investments, it will result in speedy economic development of the country and effectively contribute to achieving Cambodia’s development goals as set out in the NSDP, including the CMDGs<sup>10</sup>.

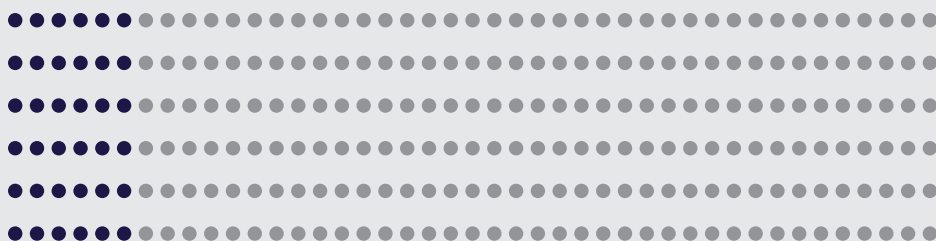


If the latter can be achieved, oil, gas and mining in Cambodia can be called a resource blessing. However, international experience highlights the risk of the ‘resource curse’, which is most likely to take place in a country whose revenue from natural resource exploitation is very big compared with its economy. The resource curse may have several features, such as corruption and rent-seeking, which divert EI income from government revenue, worsen income inequality, and exacerbate poverty, undermining political stability owing to resource mismanagement. One way to avoid the resource curse is to implement the Extractive Industries Transparency Initiative (EITI), which aims to increase transparency in transactions between governments and companies in EIs. The RGC is currently studying the EITI by means of a specialized working group. This working group is expected to make recommendations regarding the formal endorsement of EITI by the middle of 2008.

Because income from extractive industries will not last forever, it is important to invest (or save) resources wisely so that future generations will also benefit. There

<sup>10</sup> Cambodia Millennium Development Goals

is a wealth of available international experience on managing revenues from non-renewable natural resources (like oil, gas and mining). The RGC, the National Assembly and representatives of civil society should, with the support of development partners, hold an open discussion on how to use this revenue efficiently to develop the country effectively, to avoid the resource curse and to maximize the resource blessing.



## ANNEX 1 Glossary of Terms

**Amortization:** Debt amortization is the periodic amount that needs to be repaid on a loan.

**Budget:** An estimate of the annual revenue and receipts and the determined amount of expenditure and other payments by the government, approved by the National Assembly.

**Capital revenue:** Revenue from the sale of non-financial capital assets, such as land, non-material assets, commodity reserves and other items, the life of which is more than one year.

**Committed credit:** Term used in the Cambodia National Budget Law to indicate that this budget is proposed for external funding from donors; this committed credit is usually off-budget in operation.

**Decentralization & Deconcentration:** The process where certain rights responsibilities and the resources are transferred from the national level of government to democratically elected commune councils and where public services are increasingly delivered by at the sub-national level.

**Deficit:** The amount expenditure exceeds revenue in a given period.

**Direct tax:** Tax that is imposed immediately upon the taxpayer, such as tax on profits, income tax, tax on gifts and inheritances.

**Fiscal year:** A period of 12 months for which the state plans revenue and expenditure. In Cambodia, this is the same as the calendar year (January 1 to December 31).

**Gross domestic product (GDP):** The total value of all goods and services produced in a country during a single calendar year.

**Grant:** A fixed amount of funds provided by the government to local government

units (districts, communes and cities) according to measured fiscal inequality. The right can be claimed only by those local units that have below-average fiscal capacity, i.e., those that cannot cover the required budgetary spending with their own revenue.

**Indirect tax:** Tax on goods and services that is collected indirectly, via an agent such as an importer, producer or shop; examples are VAT, excise, customs duty, turnover tax.

**Payment credit:** Term used in the Cambodia National Budget Law describing the expected approved budget from the donors. Not all proposed investment programs (committed credits) are expected to be approved.

**Program credit:** Term used in the Cambodia National Budget Law describing the total budget for capital investment (funded by both domestic sources and external sources).

**Public debt:** The total indebtedness of the country to home or foreign creditors at a given moment. This represents the cumulative deficit of all levels of the budget in which the state collects and spends resources (the National Budget, the local units' budget, the budget of the extra-budgetary funds).

**Public sector:** That part of the national economy that in the widest sense comprehends all levels of government, the welfare system and public corporations.

**Revenue:** Money collected by the state. This includes taxes, fees and charges for various services, and income from the sale of state-owned capital assets.

**Surplus:** Excess of revenue over expenditure in a given period.

**Tax:** A kind of public revenue which is manifested as a forced payment to the state without there being any counter-benefit.

**Treasury:** The system of budgetary and financial management of government revenue, expenditure and the public debt. This includes the planning, execution and supervision and use of the resources of the budget.





## ANNEX 2 Further Reading and Useful Links

### Reading materials<sup>11</sup>

#### 1 Budget Law Series (1999 onwards)

The Budget Law presents expected revenues and expenditures for the new fiscal year and the expected trend of capital expenditure for the next two years. It also captures actual expenditure and revenues from the previous fiscal year. Budget Laws should be available to the public at the beginning of the new fiscal year (January) at the National Library or the libraries from the National Assembly and Senate.

#### 2 Budget Settlement Law Series (1997-2004)

The Budget Settlement Law provides an overview of the budgeted expenditures (as in the Budget Law) and compares this with actual expenditure. It further gives provides information on additional funds spent in a particular fiscal year. It should be noted that the Budget Settlement Law does not provide information how the money is spent and what outcomes have been achieved. Although the Budget Settlement Law should be prepared and made available to the public nine months after the ending of the fiscal year, this is not current practice. At the time of writing this Guide, the Cambodian Budget Settlement Law is three years behind. Like the Budget Law, the Budget Settlement Law is available at the National Library or the libraries from the National Assembly and Senate.

#### 3 Analysis of the 2007 Budget Law

The analysis assesses Government planned expenditures and compares this with previous Budget Laws and actual expenditure in both priority sectors and non-pri-

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<sup>11</sup> All reading materials and future updates are available at the Budget Project of the NGO Forum on Cambodia (please see contact details at the back of this Guide)

ority sectors. The Analysis of the 2007 Budget Law is published in the Cambodia Development Watch (Year III, No.1), available at the website of the NGO Forum on Cambodia: <http://www.ngoforum.org.kh/Development/Docs/doc.htm>

#### 4 Constitution of the Kingdom of Cambodia.

The constitution of the Kingdom of Cambodia can be accessed in the in the libraries mentioned under 1 and 2, as well as on <http://www.cambodia.gov.kh>

#### 5 Law on Audit of the Kingdom of Cambodia.

The law on audit can be accessed in the in the libraries mentioned under 1 and 2, it can be obtained at the National Audit Authority.

#### 6 Law on Financial System of the Kingdom of Cambodia.

The law on Financial System can be accessed in the in the libraries mentioned under 1 and 2.

#### 7 Cambodian National Strategic Development Plan (NSDP) 2006-210.

The NSDP is the single, overarching, guiding and reference document of the RGC and the “blue print for further progress” in building a new Cambodia (Samdech Prime Minister Hun Sen). Government and external development partners are expected to strictly adhere to the priorities set out in the NSDP. The plan can be downloaded from the web-site of the Ministry of Planning: <http://www.mop.gov.kh/>

### Useful Links

#### 1 NGO Forum on Cambodia

<http://www.ngoforum.org.kh>

The Development Issues Section accommodates various updated development documents, such as the Position Papers to the Cambodia Development Cooperation Forum (CDCF), the NGO statement to the CDCF and Cambodia Development Watch, which also contains articles on the budget and other development-related issues.

## 2 Economic Institute of Cambodia

<http://www.eicambodia.org>

This publication section of the web-site offers mostly economics-related materials, also including articles on the budget.

## 3 Ministry of Economy and Finance

<http://www.mef.gov.kh/>

The Monthly Bulletin of Statistics is published every month by the Economic and Public Finance Policy Department of MEF in order to disseminate to the public statistical information on various economics issues. The Monthly Bulletin of Statistics is available in both Khmer and English. Audiences can view the document in both languages at the same time in PDF format.

## 4 International Budget Project (IBP)

<http://www.internationalbudget.org/>

The IBP website contains a number of resources that can help groups learn more about applied budget work and connect with other civil society budget groups in developing and transitional countries. These resources include a comprehensive library, information and contact details for many of the budget groups the IBP works with, an extensive resource section, and information about the IBP's international events. The IBP also publishes a bi-monthly newsletter.

## 5 A Guide to Budget Work for NGOs

<http://www.internationalbudget.org/resources/guide/index.htm>

The Guide to Budget Work was the predecessor to this Guide on revenue work. It provides information on the principles and practices of applied budget work and an extensive list of resources for further information.

## 6 Case Studies of Six Established Budget Groups

<http://www.internationalbudget.org/casestudies.htm>

The IBP and the Institute for Development Studies conducted an extensive study of the impact of applied budget work in six countries: Brazil, Croatia, India, Mexico, South Africa and Uganda. The study concludes that the budget groups in these countries have had a significant impact in a number of areas, including enhancing budget transparency, increasing resources for pro-poor programs, and improving how these resources are used.

## 7 Open Budget Questionnaire

<http://www.openbudgetindex.org>

The IBP's Open Budget Questionnaire was developed to evaluate public access to budget information and the openness of the budget process from the perspective of civil society organizations. It focuses mainly on the expenditure side of the budget. There are, however, several questions that provide information on how revenues fit into the budget process.

## 8 IBP Electronic Library

<http://ibp.forumone.com/resources/library/index.php>

IBP's electronic library contains links to reports, studies and other documents on budget-related issues available online. It includes a section on 'Taxation and Revenue Issues'.

## 9 Extractive Industries Transparency Initiative (EITI)

<http://www.eitransparency.org/>

The EITI is led by the UK Department for International Development (DFID), in cooperation with the IMF and the World Bank. EITI aims to increase transparency in transactions between governments and companies in the extractive industries. EITI's website provides background information on the initiative, a description of the EITI principles, and information on the governments, companies and NGOs participating in the initiative.

## 10 Publish What You Pay (PWYP)

<http://www.publishwhatyoupay.org/>

PWYP is a coalition of over 300 NGOs working to improve transparency in the extractive industries. The coalition calls for mandatory disclosure of the payments made by oil, gas and mining companies to governments. The website outlines the objectives of the coalition and offers resources for groups wanting to get involved.

## 11 Revenue Watch Institute (RWI)

<http://www.revenuewatch.org/>

The RWI works with civil society, media and policymakers in resource-dependent countries to improve democratic accountability. It seeks to equip citizens with the information, training, networks and funding they need to become more effective monitors of government revenues and expenditures.

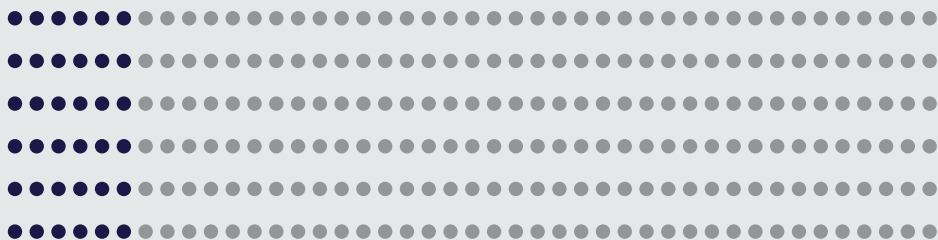












**ANNEX 4** Tables on Current and Capital Expenditures 2000-'06

Table A4.1: Budget Trends: Current Expenditure 2000-'06 (in CR Million)								
	2000	2001	2002	2003	2004	2005	2006	Increase '00-'06
Total Expenditure by Ministry	1,177,131.0	1,379,758.3	1,522,355.9	1,671,237.6	1,581,860.4	1,681,585.5	1,937,583.7	65%
General Administrative (Excl. Justice)	262,249.0	256,002.9	284,396.5	372,256.7	263,902.1	293,943.6	336,769.8	28%
Defence & Security	438,219.0	406,747.6	393,379.1	390,696.8	383,336.4	385,626.5	424,616.3	-3%
Other Sectors	116,341.0	276,433.7	273,966.2	319,879.3	321,584.8	425,518.8	491,403.3	322%
Total Priority Sectors	360,322.0	440,574.1	570,614.1	588,404.9	613,037.2	576,496.6	684,794.3	90%
Education, Youth and Sport	174,341.0	203,943.5	280,144.1	285,606.5	295,474.2	299,801.7	363,743.7	109%
Public Health	92,828.0	126,461.0	158,985.5	164,416.3	174,126.9	191,931.6	219,123.3	136%
Woman Affairs and Veteran	52,879.0	57,543.9	62,492.3	68,175.9	77,591.1	8,837.6	10,703.7	-80%
Agriculture, Forestry and Fishery	22,945.0	29,695.9	38,311.4	37,095.1	34,951.9	40,255.6	45,831.8	100%
Rural Development	7,389.0	12,126.7	17,790.1	16,065.6	15,074.3	18,923.1	24,235.1	228%
Justice	5,688.0	6,138.4	6,958.4	10,550.4	9,430.6	10,028.2	10,786.9	90%
Urbanization and Construction	4,252.0	4,664.7	5,932.3	6,495.2	6,388.0	6,718.8	10,369.8	144%

Source: Compiled from MEF Budget Implementation 2000-2006

Table A4.2: Budget Trends: Capital Expenditure 2000-'06 (in US\$ Million)								
	2000	2001	2002	2003	2004	2005	2006	Increase '00-'06
Total Expenditure by Ministry	302.2	354.2	390.8	429.1	406.1	431.7	497.5	65%
General Administrative (Excl. Justice)	67.3	65.7	73.0	95.6	67.8	75.5	86.5	28%
Defence & Security	112.5	104.4	101.0	100.3	98.4	99.0	109.0	-3%
Other Sectors	29.9	71.0	70.3	82.1	82.6	109.2	126.2	322%
Total Priority Sectors	92.5	113.1	146.5	151.1	157.4	148.0	175.8	90%
Education, Youth and Sport	44.8	52.4	71.9	73.3	75.9	77.0	93.4	109%
Public Health	23.8	32.5	40.8	42.2	44.7	49.3	56.3	136%
Woman Affairs and Veteran	13.6	14.8	16.0	17.5	19.9	2.3	2.7	-80%
Agriculture, Forestry and Fishery	5.9	7.6	9.8	9.5	9.0	10.3	11.8	100%
Rural Development	1.9	3.1	4.6	4.1	3.9	4.9	6.2	228%
Justice	1.5	1.6	1.8	2.7	2.4	2.6	2.8	90%
Urbanization and Construction	1.1	1.2	1.5	1.7	1.6	1.7	2.7	144%

**Source:** Compiled from MEF Budget Implementation 2000-2006

Table A4.3: Budget Trends: Capital Expenditure 2000-'06 (in CR Million, 2000 Constant Prices)								
	2000	2001	2002	2003	2004	2005	2006	Increase '00-'06
Total Capital Budget	1,338,660.0	1,936,514.6	1,700,558.0	1,772,264.3	1,611,905.7	1,445,023.1	1,463,233.5	9%
Other Sectors	954,252.0	1,138,562.4	1,060,975.8	1,154,028.5	945,555.8	933,134.2	987,102.9	3%
Total Priority Sectors	384,408.0	797,952.2	639,582.2	618,235.7	666,350.0	511,888.9	476,130.6	24%
Education	132,776.0	153,226.1	101,331.7	149,619.8	154,709.0	171,560.7	119,275.1	-10%
Public Health	266,737.0	450,044.8	353,923.6	358,818.4	373,737.1	282,416.2	275,419.6	3%
Woman Affairs	24,035.0	27,796.3	21,733.1	30,473.4	66,864.9	41,867.5	49,386.9	105%
Agriculture	12,532.0	128,870.4	163,283.4	148,678.7	159,778.8	115,279.5	87,502.9	598%
Rural Development	65,394.0	176,977.6	87,361.7	65,477.2	51,503.2	53,688.9	50,596.7	-23%
Justice	10,401.0	7,115.0	7,384.9	3,707.2	3,626.5	7,500.9	3,306.1	-68%
Urbanization	5,309.0	7,148.1	5,895.6	11,080.8	10,839.5	11,135.9	9,918.4	87%

**Source:** *Compiled from National Budget Law 2000-2006*

Table A4.4: Budget Trends: Capital Expenditure 2000-'06 (in US\$ Million, 2000 Constant Prices)								
Year	2000	2001	2002	2003	2004	2005	2006	Increase '00-'06
Total Capital Budget	343.7	497.2	436.6	455.0	413.8	371.0	375.7	9%
Other Sectors	245.0	292.3	272.4	296.3	242.8	239.6	253.4	3%
Total Priority Sectors	98.7	204.9	164.2	158.7	171.1	131.4	122.2	24%
Education	34.1	39.3	26.0	38.4	39.7	44.0	30.6	-10%
Public Health	68.5	115.5	90.9	92.1	96.0	72.5	70.7	3%
Woman Affairs	6.2	7.1	5.6	7.8	17.2	10.7	12.7	105%
Agriculture	3.2	33.1	41.9	38.2	41.0	29.6	22.5	598%
Rural Development	16.8	45.4	22.4	16.8	13.2	13.8	13.0	-23%
Justice	2.7	1.8	1.9	1.0	0.9	1.9	0.8	-68%
Urbanization	1.4	1.8	1.5	2.8	2.8	2.9	2.5	87%

**Source:** Compiled from National Budget Law 2000-2006





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