

Briefing Note

**PREPARED FOR COMMISSION 2 OF THE SENATE ON: FINANCE, BANKING
AND AUDIT**

The Implementation and Oversight of the Budget at the Sub-national Level

In the Context of Decentralization and Deconcentration (D&D)

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Phnom Penh, February 28 2014



Parliamentary Institute of Cambodia

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IMPLEMENTATION AND OVERSIGHT OF THE BUDGET AT THE SUBNATIONAL LEVEL IN THE CONTEXT OF DECENTRALIZATION AND DECONCENTRATION (D&D)

This briefing note provides key information to Commission 2 with regard to its Fact Finding mission from 11-14 March 2014 on the “implementation and oversight of the budget at the sub-national level in the context of decentralization and deconcentration (D&D)” in Oddar Meanchey and Siem Reap province.

D&D LEGAL BACKGROUND AND POLICY FRAMEWORK AT THE SUBNATIONAL LEVEL

The decentralization program in Cambodia is the product of decades of legal and policy reforms that find their origins in the SEILA¹ (SEILA means “foundation stone” in Khmer) program launched in 1996. After years of war and social turmoil, the initial objective of this experimental program was to layout the basis for social reconciliation and socio-economic development. However, while promoting local governance and participatory planning, a system of management for finance and rural development was established in five provinces, which expanded overtime, to all twenty-four provinces in 2003.

I. THE DEVELOPMENT OF A LEGAL AND POLICY FRAMEWORK

1. LEGAL DEVELOPMENT

The section below provides a brief overview of the legal and policy framework pertaining to the implementation and development of the D&D policy reform at the subnational level.

1.1 The Cambodian Constitution (latest update 2010)

- Article 3 states that Cambodia is a unitary state/Kingdom. The Constitution does not refer to Deconcentration and Decentralization, however Article 145 – provides that the territory of the Kingdom shall be administratively divided into Reach Theany (Royal Capital City), Khet (provinces), Krong (municipalities), Srok (districts), Khan (arrondissements), Khum (communes) and Sangkat (quarters).
- Article 51 stipulates the separation of power between the legislative, executive, and judicial branches.

¹ World Bank, Cambodia’s Seila Program: A Decentralized Approach to Rural Development and Poverty Reduction (Cambodia: World Bank, 2004), p.1.

- Article 146 provides that Reach Theany, Khet, Krong, Srok, Khan, Khum and Sangkat are administered according to the conditions provided by the organic law.

1.2 The Law on Provincial and Municipal Budgets and Asset Management Regime (1998)

This law represents the basis for the subnational administration finance law currently drafted. It is currently in use and allows governors and deputy governors to manage budgets and assets on behalf of the central government².

1.3 The Law on Commune and Sangkat Administrative Management (2001)

This law established the administrative management of all Khum-Sangkats in the Kingdom of Cambodia following the policy of decentralization. This Law stipulates that each Commune shall have a Council, called a “Commune Council.” Each council has the power to manage the local affairs of their communes. It is important to note that Article 4 of this Law provides that the governing and managing powers of the Communes (Khum-Sangkat) derive from direct elections. In addition, Article 11 stipulates that the Commune Council is directly elected by the citizens of its commune for a five year mandate.

1.4 The Organic Law on the Administrative Management of Capital, Provinces, Municipalities, Districts and Khans (2008)

This Law is very important to the D&D framework: Article 8 specifies the Capital, Provinces, Municipalities, Districts and Khans as legal entities of the public laws to be governed in accordance with the principle of a unified administration. Each subnational level shall implement, promote and sustain democratic development through the policy of decentralization and deconcentration. However, unlike the communes, Article 14 of the Organic Law states that the Councils of the Capital, Provinces, Municipalities, Districts and Khans are indirectly elected in accordance with the procedures in the Law on Elections of the Capital council, Provincial council, Municipal council, District council and Khan council.

2. POLICY FRAMEWORK

From a national policy perspective, the Royal Government of Cambodia (RGC) launched the Decentralization and Deconcentration Strategic Framework (D&D strategy) in 2005 with the principal objectives to improve the provision of public service, further fiscal decentralization, and set up the legal framework to increase own-source revenues at the commune levels. The 2005 framework of this strategy is the basic document that guided the development of the 2008 Organic Law.

² Tariq H. Niazi, Deconcentration and Decentralization reform in Cambodia (Philippines: Asian Development Bank, 2011), p.101.

In addition to the legal framework and to reinforce the 2005 D&D strategy, the National Program for Sub-National Democratic Development (NP-SNDD) was designed in 2010 and officially adopted by the Council of Ministers. The NP-SNDD mapped out the RGC's agenda for the next 10 years in order to implement the D&D strategy.

Five Programme Areas were identified as follows:

1. Sub-national Institutional Development;
2. The Development of Strong Human Resource Management Systems;
3. The Transfer of Functions and Resources;
4. Sub-National Budget, Financial and Property Systems; and
5. Support Institutions for the D&D Reform Process.

However, the roles, authorities, and functions of various levels of government lack clarification. In 2010, the National Committee for Sub-National Democratic Development (NCDD)³ designed the first Three-Year Implementation Plan (IP3, 2011). The NCDD is an inter-ministerial body created to support the ministries at the technical level and coordinate the various ministries' work to implement the first three years of the NP-SNDD. Nevertheless, the IP3 is a very complex and ambitious program to implement by all of the various stakeholders. In addition the coordination/cooperation between various ministries remains challenging. As a result, many of the activities are behind in terms of implementation.

II. THE FINANCIAL SYSTEM

The following section briefly describes the Laws related to the financial system in Cambodia, including the Organic Law (2008), the Law on Public Finance Systems (2008) and the Draft Law on Financial Regime and Management of Assets of Sub-national Administrations (2008 latest update).

It should be noted that there are some inconsistencies between the Organic Law and the Law on Public Finance Systems as follows:

The Organic Law provides more autonomy to the elected councils to manage their budget and local fiscal and non-fiscal revenue as described in Article 244 below:

- *"the Capital council, Provincial council, Municipal council and District council have the right to receive revenue from local, national and other sources of revenue in accordance with the Law on Financial Regime and Management of Assets of Sub-national Administrations that has been formulated in consistence with this Law and the Law on Public Financial System."*
- *"Khan councils and Sangkats council have a budget to carry out their functions and duties, which shall be included in the budget of the Capital and Municipal councils"*

³ The NCDD is an inter-ministerial body responsible for the design and implementation of decentralization and deconcentration policies. See <http://www.ncdd.gov.kh/en/about-ncdd>

On the other hand, the Law on Public Finance Systems provides more of a centralist approach to budget management and supervision.

- Article 34 and Article 35 provide that the Governor shall prepare the budget strategic plan and budget for the SNAs in accordance with the calendar and the guidelines determined by the Ministry of Economy and Finance (MEF) and following the circulars the MEF issues.
- More specifically, Article 35 stipulates that:
 - Article 35(1). The budget Strategic Plan be prepared from March to May of each year;
 - Article 35(2). The budget package be prepared from June to September of each year; and
 - Article 35(3). The budget of the SNAs be adopted from October to December of each year.

Furthermore, in the first week of October of each year, the MEF submits the budget plan of the SNAs to the Council of Ministers for review and approval. The budget plan represents one chapter of the draft annual national budget law. It is then submitted to the National Assembly for approval in the first week of November, then to the Senate for final endorsement in the first week of December. The final endorsement of the budget plan shall take place by 25th of December each year.

The inconsistencies between the Organic Law and the Law on Public Finance Systems will hopefully be addressed with the Law on Financial Regime and Management of Assets of Sub-national Administrations (SNA) currently being drafted (latest update 2008). Indeed, this new Law will further define the responsibility and management of finance and property of SNA; the budget and budget's management; liabilities; the preparation, adoption and execution of SNA budget; as well as the management of the SNAs' properties.

Regarding the Draft Law on Financial Regime and Management Assets of Subnational Administrations:

- Article 15 of this draft Law provides that the Treasury of the subnational administration act as Public Accountant for the subnational administration and shall be responsible for the following tasks:
 - Collecting or receiving revenues for subnational administrations;
 - Executing payment orders issued by the Governor of the subnational administration;
 - Managing and releasing funds for the subnational administration;
 - Preparing financial reports on a regular basis; and
 - Filing and safeguarding all documents supporting transactions and accounting records of a subnational administration.
- Article 16 of this draft Law stipulates that the Director of the Department of Economy and Finance, the Director of the Treasury, the Director of the Tax Branch or Tax Office located within each jurisdiction of the SNA receive delegated powers from the MEF to support the SNA and Board of Governors to implement the Law.

III. DEVELOPMENT PARTNERS AND THE D&D REFORM

While there have been many development partners involved in supporting the D&D reform in the past decade, this section focuses on the Asian Development Bank (ADB), which has been a strong financial and technical supporter of the D&D reform since 2003. Indeed, according to the ADB report (2011), it has contributed approximately \$85.4 million, of which \$68 million were grants allocated to development aid projects.⁴ While one project entitled “Public Financial Management for Rural Development Program, Grant for Sub-Program (SP1) and Grant Assistance” is related to the Public Financial Management for rural development, the rest of the projects are more related to local economic development mainly in the Tonle Sap region, Battambang and Siem Reap provinces.

In the ADB “Deconcentration and Decentralization” report (2011), the author cites several issues connected to the implementation of these projects. Following the results of the case studies reviewed by ADB,⁵ a few points are summarized here:

- The Tonle Sap Sustainable Livelihoods Project allocated grants to 37 communes through the Community Livelihood Fund (CLF) to improve social infrastructure, and help create income generation and community fishing activities. Because of the restricted number of communes that benefited from the CLF, this led to an increased horizontal inequity in grants funding between the communes, which hindered government’s efforts for equalization. Furthermore, the CLF included very high overheads costs for the external consultants through subsidized wages.
- Ineffective implementation of the projects: ADB and the SNAs have different approval, accounting, audit and reporting rules. This led to a duplication of work especially given the limited resources available.
- Donors’ projects approach versus institutional program approach: as most of the DP’s activities are conducted on a project basis with limited resources and timeframe, this contradicts the national institutional program’s approach, which has the objective to achieve long term sustainability and accountability at various levels of SNAs.
- External audits of the communes shall be strengthened under the National Audit Authority, including the specifics of DP’s grants.

Furthermore, DPs such as UNICEF, UNDP, GIZ and EU Space have also played consultative roles for key ministries, including Education, Health and Planning. However, the cooperation of these DPs to support the D&D reform is often perceived as fragmented and difficult to coordinate.

⁴ Tariq H. Niazi, Deconcentration and Decentralization reform in Cambodia (Philippines: Asian Development Bank, 2011), p.86-94.

⁵ Ibid. p,85-86,88.

IV. CONCLUSION

While significant progress has been made over the past decades towards D&D, the reform remains very complex to implement. Two major components need to be addressed to ensure the progress of the reform. Firstly, the functional assignment at the various levels of SNAs needs to be clarified and completed. Secondly, the SNA's financing regulatory framework and capacity building for financial management and accountability needs to be clarified and finalized (SP4, IP3, 2011). These two important aspects of the reform are essential to the successful development and implementation of the D&D reform moving forward. Furthermore, while DPs have brought considerable support, both technically and financially, to the advancement of the D&D reform, some issues have been raised as briefly described above, including those of project approach versus the broader national program approach.

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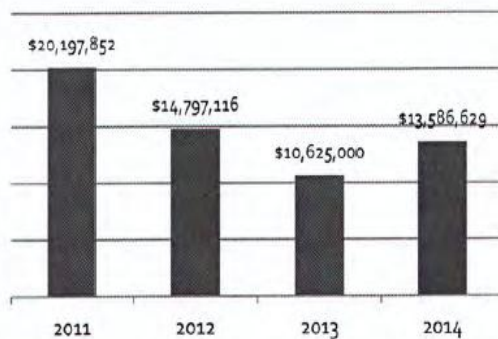
APPENDICES

Appendix I: Annual Work Plan and Budget for 2014

The 2014 AWPB budget

PLANNED EXPENDITURES

2014 AWPB planned expenditures, financed through the basket fund, are budgeted at **\$13,586,629**. This is an increase of 28% over 2013. Including the IP₃ extension and over the program's four years of implementation, planned expenditures reached \$59.21 Million as opposed to a figure of \$68.84 Million, as found in the IP₃ document (i.e. 14% less than expected). Though operating at a somewhat reduced level and over a longer period of time, resources are considered adequate to produce most of the outputs identified in the IP₃.



Source: IP₃ Extension 2014 of NP-SNDD, 2014 Annual Work Plan and Budget

Appendix II: Expenditure of Sub-program1-4

Table 1: Overview of Planned 2014 Expenditures

SP	A. Basket	% Basket	B. Earmarked	C. Fiscal Transfers	Total (A+B+C)	% Total
Sub-Program 1	\$4,835,299	35.59%	\$17,862,525	\$0	\$22,697,824	8.22%
Sub-Program 2	\$575,494	4.24%	\$4,740,820	\$0	\$5,316,314	1.93%
Sub-Program 3	\$356,820	2.63%	\$0	\$0	\$356,820	0.13%
Sub-Program 4	\$175,357	1.29%	\$5,004,044	\$233,863,704	\$239,043,105	86.59%
– Reform Activities	\$175,357		\$1,004,044	\$0	\$1,179,401	0.43%
– Fiscal Transfers	\$0		\$4,000,000	\$233,863,704	\$237,863,704	86.16%
Sub-Program 5	\$45,490	0.33%	\$139,000	\$0	\$184,490	0.07%
Sub-Program 6	\$120,520	0.89%	\$389,682	\$0	\$510,202	0.18%
SNAs (PC/DMK expenditures)	\$7,477,649	55.04%	\$491,328	\$0	\$7,968,978	2.89%
Total	\$13,586,629	100.00%	\$28,627,399	\$233,863,704	\$276,077,733	100.00%
%	4.92%		10.37%	84.71%	100.00%	

NOTE: ALL CALCULATIONS EXCLUDE IN KIND ACTIVITIES. FISCAL TRANSFERS ARE FINANCED BOTH BY THE RGC AND SIDA. SP1 EARMARKED FUNDS INCLUDE A \$125,000 CONTRIBUTION BY THE RGC TO NCDD.

As can be seen above, earmarked expenditures remain 2.1 times as large as discretionary basket funded expenditures. Within the basket, about 55% of all funding goes to SNAs. Data for fiscal transfers is provided in table 2.

Table 2: Expected Fiscal Transfers 2014

Fund	Sida	RGC	Total
CS Fund	\$0	\$58,584,198	\$58,584,198
DM Fund	\$4,000,000	\$17,047,901	\$21,047,901
CP Budget	\$0	\$158,231,605	\$158,231,605
Total	\$4,000,000	\$233,863,704	\$237,863,704

Source: IP3 Extension 2014 of NP-SNDD, 2014 Annual Work Plan and Budget

Appendix III: Financial Status

Figure 3: Status /Progress of 2012 AWPB Outputs

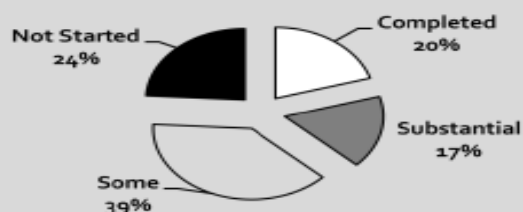


Table 1: Financial Data (excluding fiscal transfers)

ITEM	BUDGET	EXPENDITURE	%
CENTRAL IMPLEMENTERS	\$10,972,723	\$10,289,758	93.8%
Sub Program 1 (NCDD-S)	\$4,320,152	\$4,120,911	95.4%
Sub Program 2 (MOI)	\$1,234,944	\$1,003,170	81.2%
Sub Program 3 (SSCS)	\$156,352	\$55,591	35.6%
Sub Program 4 (MEF)	\$4,838,137	\$4,832,047	99.9%
Sub Program 5 (MOP)	\$183,616	\$89,337	48.7%
Sub Program 6 (LEAGUE)	\$239,523	\$188,702	78.8%
PROVINCES/CAPITAL	\$8,371,334	\$8,041,447	96.1%
Banteay Meanchey	\$336,359	\$313,342	93.2%
Battambang	\$477,134	\$443,799	93.0%
Kampong Cham	\$609,931	\$609,241	99.9%
Kampong Chhnang	\$346,005	\$335,392	96.9%
Kampong Speu	\$381,363	\$359,485	94.3%
Kampong Thom	\$387,119	\$381,490	98.5%
Kampot	\$355,811	\$321,384	90.3%
Kandal	\$457,420	\$453,502	99.1%
Kep	\$162,739	\$145,259	89.3%
Koh Kong	\$277,403	\$263,970	95.2%
Kratie	\$297,811	\$284,794	95.6%
Mondul Kiri	\$260,167	\$261,153	98.1%
Oddar Meanchey	\$166,931	\$253,891	97.6%
Pailin	\$379,176	\$166,582	99.8%
Phnom Penh	\$230,031	\$372,925	98.4%
Preah Sihanouk	\$310,807	\$202,273	87.9%
Preah Vihear	\$504,275	\$306,074	98.5%
Prey Veng	\$291,600	\$498,747	98.9%
Pursat	\$352,450	\$288,577	93.9%
Ratanak Kiri	\$448,748	\$330,890	89.0%
Siemreap	\$285,103	\$399,369	96.5%
Stung Treng	\$384,619	\$275,225	98.8%
Svay Rieng	\$402,082	\$380,100	98.0%
Takeo		\$393,983	94.8%
Total	\$19,344,057	\$18,331,205	94.8%

Source: NCDD (Phnom Penh: IP3 Annual Implementation Report January to December 2012, 2013), 2.

Appendix IV: Sources of Funds

Table 27: Sources of funds

Source/Balance	Amount	% budget	% balance
1. Total available funds (budget)	\$19,344,057	100.00%	
1.1. Sida	\$17,518,070	90.56%	
1.2. UNICEF	\$1,690,717	8.74%	
1.3. UN Women	\$39,888	0.21%	
1.4. ADB	\$64,140	0.33%	
1.5. WB-OWSO	\$31,243	0.16%	
1.6. Other income (include c/f \$4,683.10)	\$4,784	0.02%	
2. Actual Expenditure	\$18,331,206		
3. Balance: Estimated Carry Over to 2013 (item 1- item 2)	\$1,012,851		100.00%
3.1. SIDA	\$658,721		65.04%
3.2. UNICEF	\$332,154		32.79%
3.3. UN Women	\$21,977		2.17%
3.4. ADB	\$0		0.00%
3.5. WB-OWSO	\$0		0.00%
3.6. Other income	\$4,784		0.47%

Source: NCDD (Phnom Penh: IP3 Annual Implementation Report January to December 2012, 2013), 34.

Appendix V: Annual Work Plan and Budget 2013

Table 1: The IP3 Basket Fund Budget over Time

Year	A. IP3 Budget	B. Actual Budget	% (B ÷ A)	* Reduction
2011	\$30,163,891	\$20,197,852	67%	
2012	\$21,639,356	\$14,797,116	68%	27%
2013	\$17,040,191	\$10,625,000	62%	29%
Total	\$68,843,438	\$45,619,968	66%	

* Reduction from previous year

Table 2: 2013 AWPB Budget Overview

CATEGORY	RGC	DPs	TOTAL	%
1. IP3 Program Contributions	\$65,019,568	\$14,500,000	\$79,519,568	35%
1.1. Basket Fund for SPs/SNAs	\$125,000	\$10,500,000	\$10,625,000	5%
1.2. CS Fund	\$50,473,580		\$50,473,580	22%
1.3. DM Fund	\$14,420,988	\$4,000,000	\$18,420,988	8%
2. Earmarked	\$963,262	\$16,820,610	\$17,783,872	8%
3. In-Kind		\$4,891,465	\$4,891,465	2%
4. PC Budget	\$124,001,234		\$124,001,234	55%
TOTAL (1+2+3+4)	\$189,984,064	\$36,212,075	\$226,196,139	100%

Table 3: DP Source of Funds

FUNDING SOURCE	PROGRAM	earmarked	IN-KIND	TOTAL
Sweden/SIDA	\$11,500,000			\$11,500,000
EU	\$3,000,000			\$3,000,000
ADB/PPTA		\$403,000		\$403,000
ADB/DPFSM		\$1,500,000		\$1,500,000
EU-SPACE			\$1,500,000	\$1,500,000
Japan/JICA-PILAC			\$913,409	\$913,409
UNDP			\$944,056	\$944,056
AusAid			\$500,000	\$500,000
UNICEF		\$1,125,690	\$1,034,000	\$2,159,690
UNCDF		\$547,450		\$547,450
UNFPA		\$343,789		\$343,789
UN/Women		\$54,000		\$54,000
ADB/TS-PRSDP		\$6,250,691		\$6,250,691
WB-OWSO		\$1,740,392		\$1,740,392
WB-LASED		\$4,855,598		\$4,855,598
TOTAL	\$14,500,000	\$16,820,610	\$4,891,465	\$36,212,075

Source: IP3 NCDD (Phnom Penh: 2013 NCDD Annual Work Plan and Budget, 2013), 4.