

The Provincial Business Environment Scorecard in Cambodia

A Measure of Economic Governance and Regulatory Policy



November 2009

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Abbreviations

| | |
|----------------|---|
| ADB: | Asian Development Bank |
| CDRI: | Cambodian Development Resource Institute |
| DANIDA: | Danish International Development Agency |
| DFID: | United Kingdom's Department for International Development |
| DIME: | Department of Industry, Mines, and Energy |
| DOC: | Department of Commerce |
| DOT: | Department of Tourism |
| ICA: | World Bank's Investment Climate Assessment |
| IFC: | International Finance Corporation |
| LMAP: | Land Management and Administration Project |
| MDLF: | Multi-Donor Livelihoods Facility |
| MIME: | Ministry of Industry, Mines and Energy |
| MOC: | Ministry of Commerce |
| MOT: | Ministry of Tourism |
| MPDF: | Mekong Private Sector Development Facility |
| MSME: | Micro, small, and medium enterprises |
| NZAID: | New Zealand's International Aid & Development Agency |
| OWS: | One Window Service |
| PBES: | Provincial Business Environment Scorecard (PBES) |
| VAT: | Value added tax |
| WB: | World Bank |

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1. Introduction

In Kratie Province, a window and door shop owner states: “In my province, provincial officials do not support business activities. They never visit or invite us to talk about our business environment problems.” However, in the neighboring province of Kampong Cham, the owner of a small brick factory feels that his province’s business climate has improved. “Bribes have declined sharply. A reduction in administrative procedures has helped to reduce corruption.”

As these stories indicate, entrepreneurs’ experiences with local authorities can vary dramatically from one Cambodian province to another. While laws and regulations are decided at the national level, how they are understood and implemented depends very much on provincial authorities. Differences in the quality of economic governance² from one province to another contribute to uneven levels of growth across Cambodia.

In order to understand how provinces are supporting or preventing business growth, International Finance Corporation and The Asia Foundation have collaborated in developing the Provincial Business Environment Scorecard (PBES). The 2009 PBES ranks all 24 provinces on the quality of their economic governance.

The PBES provides reliable data to help businesses and local governments identify which governance factors are most in need of improvement. This evaluation is particularly

important because it will help Cambodia’s micro, small, and medium enterprises (MSMEs), which represent over 95 % of private enterprises, to achieve their potential in creating jobs in rural areas where the majority of Cambodians live and poverty rates are highest. Creating jobs is more important than ever with 230,000 young people joining the labor market every year³.

The PBES, which covered 10 Cambodian economically important provinces in 2006, and all 24 provinces in 2009, relies largely on the perceptions of business owners to generate a scorecard that ranks provinces on measures of business environment quality. In this way, the PBES helps public officials identify province specific areas for reform.

The PBES also gives business owners the evidence they need to advocate effectively for reforms and engage public officials in productive discussions about how to achieve reforms. Numerous obstacles such as lack of information on regulations, time consuming procedures, unofficial charges, and the poor delivery of essential public services all hamper business growth.

In addition to pointing out areas for reform, the PBES identifies provinces engaging in good practices so that other provinces can learn from these examples. Also, 2006 PBES and 2009 PBES provide a baseline against which policymakers and regulators can monitor the results of reforms over time.

² Economic governance refers to the nature and practice of economic management, regulation and development; or the institutional environment that governs economic activities.

³ Cambodia Economic Watch, Economic Institute of Cambodia (April 2005).

2. Provincial Business Environment Scorecard and Sub-indices

2.1. Overall Scoring Strategy

The PBES scores are generated through a mixture of responses to survey questions and ‘hard’ data collected from government sources and other published materials. These data are all grouped into 10 broad sub-indices (categories), which are assessed on a 1-10 point scale. Added together, these 10 sub-indices create a 100-point overall score for economic governance. Technically, it is possible for a province to receive a perfect score of 100 if it earns top scores on all 10 indicators, however, perfection is very difficult to achieve. Indeed, all provinces have low scores in some areas.

Before describing the sub-indices and the survey strategy, it is important to note that the sub-index rankings are based on how provinces perform relative to other provinces on particular survey questions and other data. Therefore, the point totals are not comparable to point totals in other countries or some ideal measure of governance. Rather, the sub-indices should be viewed as measures of comparative achievement of provinces in the Cambodian context. For a more detailed explanation of the scoring strategy, see Chapter 8 of this report.

2.2. The Sub-indices

The following 10 sub-indices were used to grade all 24 of Cambodia’s provinces.

1. Entry Costs: A measure of the time it takes for firms to register and receive all the necessary licenses to start a business; the number of licenses required; and the official costs of registering and obtaining all required licenses/permits.

2. Property Rights: A measure of the formal rights businesses have to the land and buildings they occupy and their security of tenure once land is properly acquired and titled.

3. Transparency: A measure of whether firms have access to the information they need about government regulations and procedures, as well as the related legal documents necessary to run their businesses; whether regulatory information and legal documents are available to everyone who asks; and whether new policies and laws are communicated to firms and enforced in a predictable manner.

4. Time cost of regulatory compliance: A measure of how much time firms spend on complying with government regulations, how long they wait for procedures to be completed, as well as how frequently firms are inspected by local government agencies.

5. Informal Charges/Bribes: A measure of how often firms pay informal charges such as bribes and kickbacks to obtain government

contracts; the extent to which these informal payments are obstacles to business operation, and whether informal payments are predictable and achieve the expected results.

6. Participation: A measure of whether firms are consulted about proposed provincial policies and whether business associations or other interest groups advocate on behalf of business owners.

7. Crime Prevention: A measure of how much firms pay in costs that result from theft as well as the costs to prevent crime by paying for security services and/or ‘protection money’.

8. Tax Administration: A measure of both administrative procedures related to paying tax and the cost of tax in the province.

9. Proactivity of Provincial Leaders: A measure of the creativity and willingness of provincial authorities to interpret national policies and regulations in favor of local private firms and develop their own provincial initiatives to promote private sector development.

10. Dispute Resolution: A measure of firms’ satisfaction with the outcomes of formal and informal methods of dispute resolution in their province⁴.

2.3. Survey Strategy

Each sub-index is based primarily on responses to survey questions answered by Cambodian business owners in the 2009 PBES. To ensure that the results accurately reflect conditions throughout the country, sophisticated survey and sampling techniques were used to ensure that no region or type of business was over or under-represented, and that survey questions generated meaningful responses. In total, 1,234 business owners from all 24 provincial capitals plus ten economically important districts across the nation were surveyed.

Among the randomly selected 1,234 interviewees, the PBES also interviewed representatives from 152 firms that participated in the 2006 PBES survey. These previously interviewed entrepreneurs were critically important in 2009 PBES because they experienced the business environment in 2006 and could directly compare this with conditions two years later. This provided the best opportunity to compare changes in economic governance over time.

For a more detailed description of how the survey and sampling were conducted and how the panel respondents were selected, see Chapter 8, Section 1.

⁴ Detailed lists of the indicators used in each Sub-index can be found in Appendix 1.

3. Profile of Cambodian Firms

To help understand the results of the PBES survey, it is useful to look at the listing of businesses from which survey respondents were drawn. Since exhaustive and comparable lists of businesses in Cambodia's 24 provinces had not been made, the PBES research team gathered basic information on MSMEs in the capital city of each province, plus one additional district in Cambodia's 10 most economically active provinces. Counting all businesses operating within three kilometers of the center of each provincial capital and in selected districts added up to a total of 63,507 firms. Of these businesses, 95.5% agreed to provide the information requested by the research team so the data in the listing are extremely reliable.

Because we only counted businesses within provincial capitals and selected districts, we cannot claim that our listing covers all businesses in Cambodia. Since we only included 10 districts, in addition to provincial capitals, there is a slight urban bias to the findings. Also we have likely missed some large manufacturing establishments (particularly in food processing) that are located more than three kilometers from the center of town. That said, the listing of businesses created for the PBES is certainly the most comprehensive listing of businesses to date and systematic data collection procedures mean that data is directly comparable across Cambodian provinces. Also, the listing of more than 63,507 businesses in all 24 provinces, served as an ideal sample frame for randomly

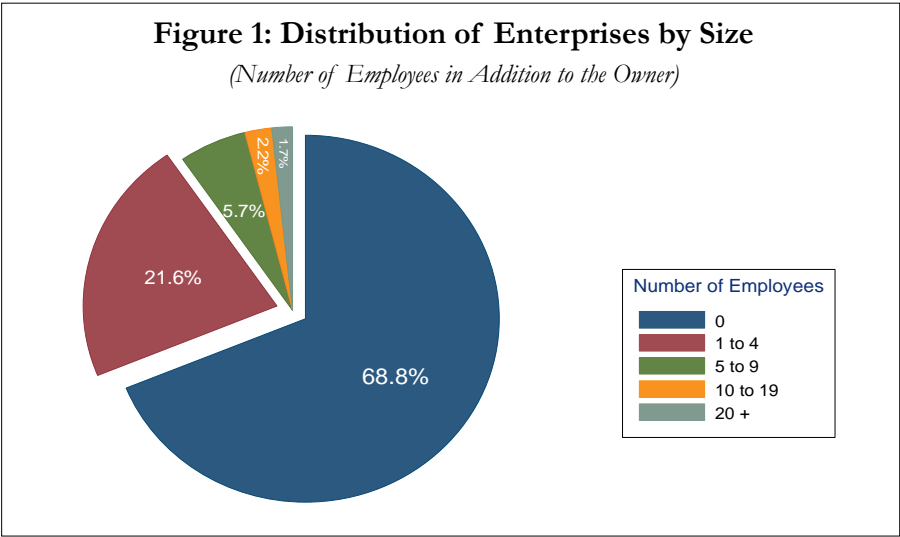
selecting the 1,234 entrepreneurs who were surveyed for the 2009 PBES.

Before examining how the index was constructed, it is helpful to review some key features of Cambodia's private sector. First, while private sector development attracts a lot of attention, very little statistical information is currently available on Cambodia's private enterprises. What do Cambodian businesses look like? By providing a valuable profile of Cambodia's private sector, the listing and descriptive information from the survey provide general answers. Second, a more accurate picture of the Cambodian business environment will provide a framework for understanding the needs of specific business environments. Third, and most important for this report, a picture of the nation's firms provides more context regarding who responded to the survey which was used to generate the PBES scorecard.

3.1 Cambodia's Firms are Micro-enterprises

The most striking finding from the listing of almost 64,000 businesses across Cambodia is the very small size of most firms. For 69% of businesses, the only employee is the owner, 90.4% of enterprises in the listing have fewer than four employees, and 96% have fewer than 10 (Figure 1). If one refers to the general definition of a micro-enterprise as an enterprise with less than 10 employees⁵, then 96% of Cambodian businesses are micro-enterprises.

⁵ Definition used by the Ministry of Industry, Mines and Energy.



While this report uses the terms ‘MSMEs’, ‘firms’, ‘enterprises’ and ‘establishments’ interchangeably, readers should keep in mind that 96 % of firms are micro-enterprises. Table 1 compares the 2006 and 2009 PBES listings in order to study changes in the business community over time. Overall, the distribution of enterprises by size has changed only slightly since 2006. Businesses with fewer than four employees still make up the vast majority of enterprises (92% in 2006 and 89% today).

3.2 Increase in Small and Medium Enterprises ⁶

Overall, more businesses are opening in Cambodia. If we look just at the firms surveyed in the 10 provinces covered by the 2006 listing (hereafter referred to as the ‘Original 10’), we see that the total number of businesses grew by 27% in the past two years. Although there

were some differences in the methods used in the 2006 and 2009 PBES to generate the listing of businesses⁷, the difference would probably lead to an underestimate of the extent of business growth. It is clear that more and more entrepreneurs are taking the risk of starting a business, and moreover, the growth rate was highest for larger businesses. The number of business with between 10 and 20 employees has nearly doubled over the past two years, while those with over 20 employees grew by almost 200%. Both of these trends, while still at an early stage, should contribute to employment growth and poverty reduction in the long run.

3.3 Concentration of Firms in the Phnom Penh Region is Decreasing

As Figure 2 demonstrates, the listing shows a strong concentration of enterprises in the capital city and surrounding provinces. Phnom

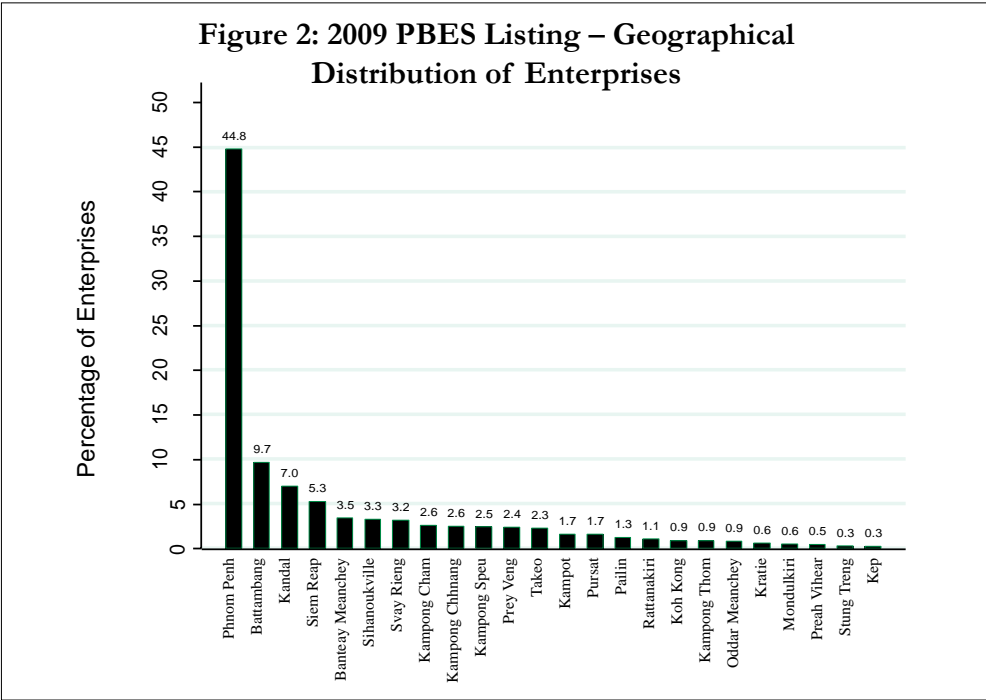
⁶ For a detailed analysis of changes in firms and how the numbers were re-weighted to reflect population differences between provinces, see Chapter 8, Table 36.

⁷ The 2006 PBES counted all businesses in the three largest districts and capital of a province, while the 2009 PBES only considered enterprises in the capital city and one additional district in each of Cambodia’s 10 most economically active provinces.

Table 1: Changes in Distribution of Enterprises by Size (2006 and 2009 PBES)

| Firm Size (Employees) | 2006 | 2006 (%) | 2009 Original 10 Provinces | 2009 Original 10 (%) | 2009 Full | 2009 Full Share | Growth in Original 10 |
|-----------------------|--------|----------|----------------------------|----------------------|-----------|-----------------|-----------------------|
| 0 (Only Owner) | 29,841 | 71.4% | 35,778 | 67.3% | 43,709 | 68.8% | 19.9% |
| 1 to 4 | 8,703 | 20.8% | 11,755 | 22.1% | 13,689 | 21.6% | 35.1% |
| 5 to 9 | 2,126 | 5.1% | 3,270 | 6.2% | 3,597 | 5.7% | 53.8% |
| 10 to 20 | 733 | 1.8% | 1,304 | 2.5% | 1,424 | 2.2% | 77.9% |
| 20 and over | 372 | 0.9% | 1,021 | 1.9% | 1,088 | 1.7% | 174.5% |
| Total | 41,775 | 100% | 53,128 | 100% | 63,507 | 100% | 27.2% |
| Employment Per Firm | 2.01 | | 2.32 | | 2.08 | | 15.4% |

The 2006 and 2009 comprehensive PBES listing varied slightly in sampling methodology. In 2006, the most populous three districts in each province were counted. In 2009, only the capital and one district in 10 economically-active provinces were counted.



Penh accounts for 45% of all enterprises. While this is a substantial share, it is much smaller than in 2006, where Phnom Penh accounted for 60% of businesses. In the current listing, Battambang comes far behind Phnom Penh with 10% of all enterprises listed, and Phnom Penh’s neighboring province, Kandal, has 7% of businesses. The high percentage of businesses concentrated in Phnom Penh is comparable to that in other capital cities in developing countries in Southeast Asia and beyond.

3.4 Firms Tend to Operate only within Their Home Province

Not only are businesses small, they are also quite ‘provincial’. Ninety percent of surveyed businesses operate solely within their home province, and only 10% export. Businesses in Phnom Penh are more sophisticated than those in other parts of Cambodia, with 16% of firms engaged in exporting⁸.

⁸ As a result of Phnom Penh’s disparity and its under-representation in the national sample, the nationally-weighted sample differs slightly from the PBES sample. See Table 36 for more details.

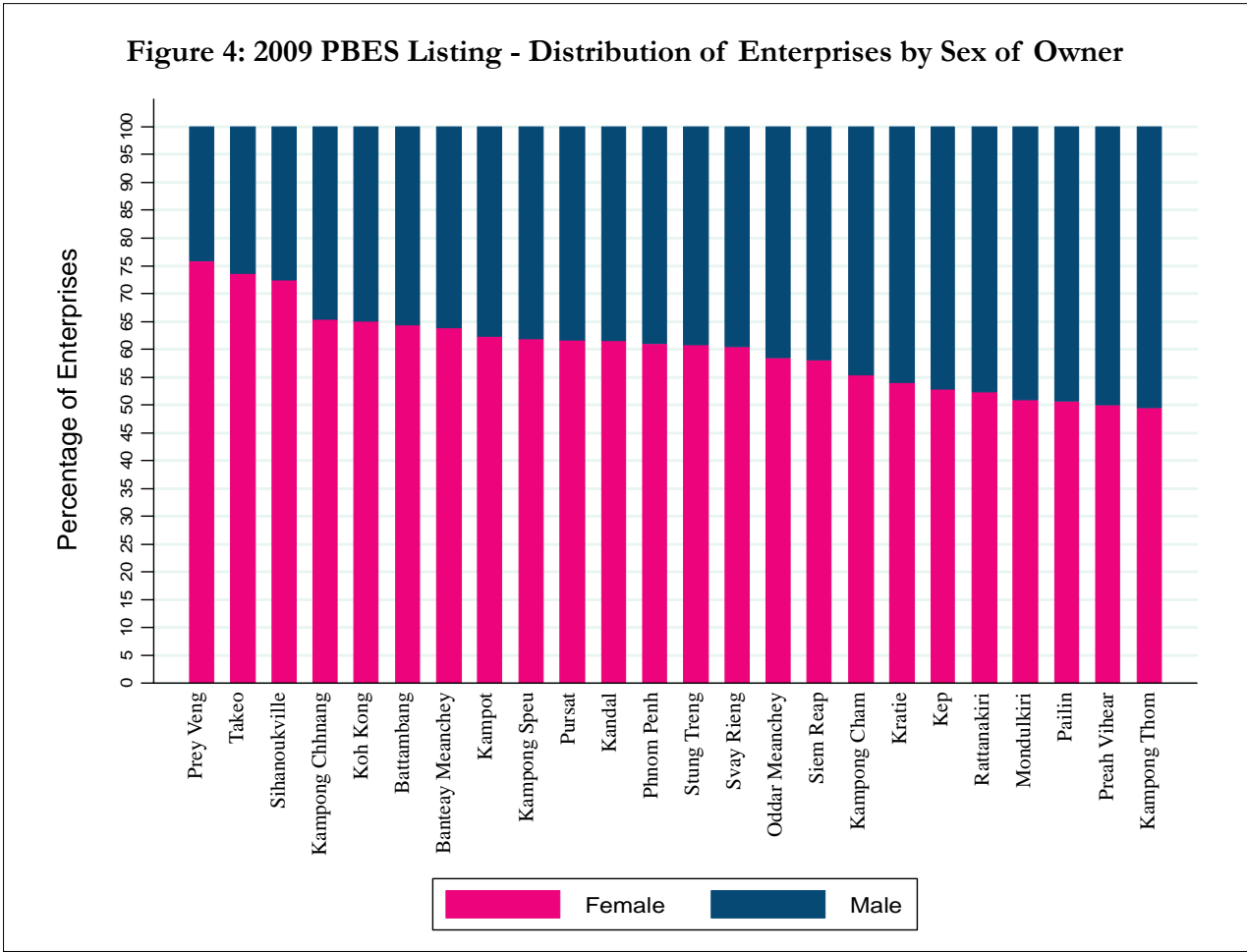
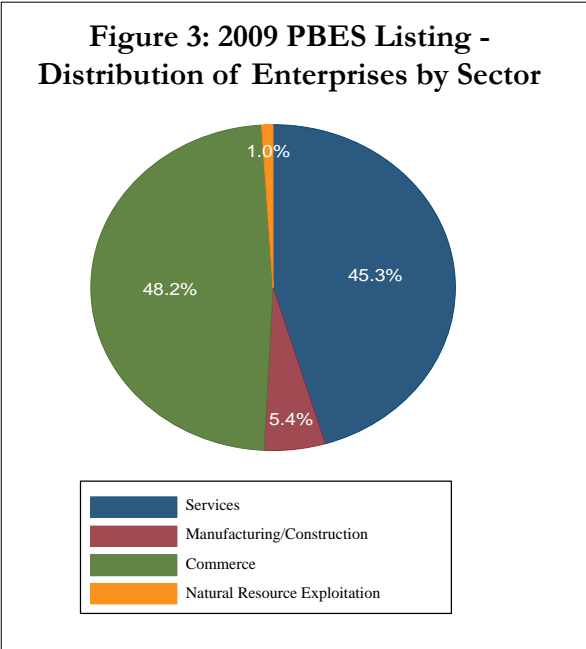
3.5 Most Firms are in Services or Commerce

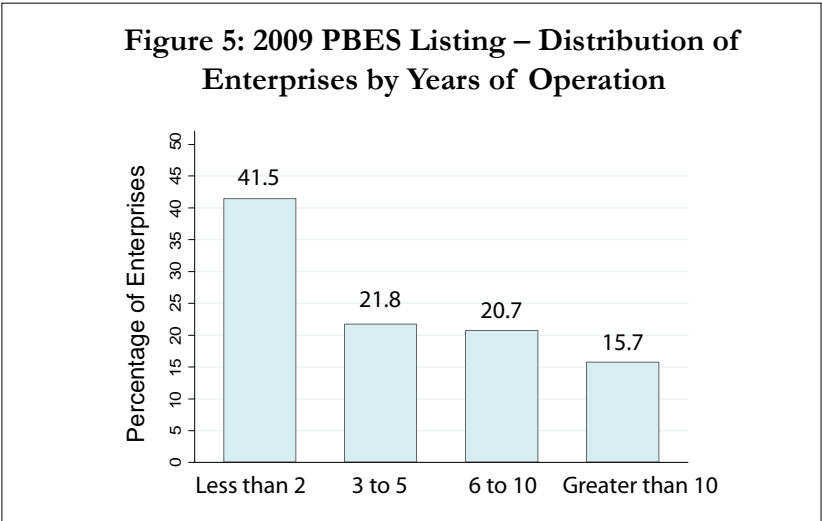
If we disaggregate by sector, both the listing and the PBES survey show that 93.5% of enterprises are concentrated in services or commerce (48.2% and 45.3%, respectively), while manufacturing and construction account for only 5.4%, and natural resource exploitation account for only about 1%. Figure 3 displays this data from the comprehensive business listing.

3.6 Women are Active in Business

The important role that women play in the private sector is shown in Figure 4. With women owning 62% of listed enterprises, their role in economic growth is substantial. However, gender distribution varies tremendously by province, with Prey Veng, for example, showing

a large percentage of women business owners (almost 75%).





3.7 Firms are Young

Finally, the listing shows that the majority of the enterprises listed are young. Forty-two percent of businesses have operated for less than two years, while another 22% have operated for less than five years (Figure 5). This indicates dramatic growth in entrepreneurial activity over the past few years. This result has critical implications for analysis of the survey results. As shown in Section 4.6 of this report, the rapid growth of new start-ups in the past few years means that many firms have only just begun operations,

and have not yet registered their enterprise and joined the formal sector.

3.8 Business Growth is Likely to Continue

Drawing on data from the PBES survey, it seems likely that rapid growth in the private sector will continue. Forty-nine percent of businesses surveyed for the PBES intend to increase their business activities over the next two years. However, these figures should be treated with some caution as the survey was conducted before the international financial crisis began in late 2008.

4. The 2009 PBES Rankings: Explanation and Analysis⁹

The following sections show the PBES rankings and discuss them in the context of Cambodian economic development.

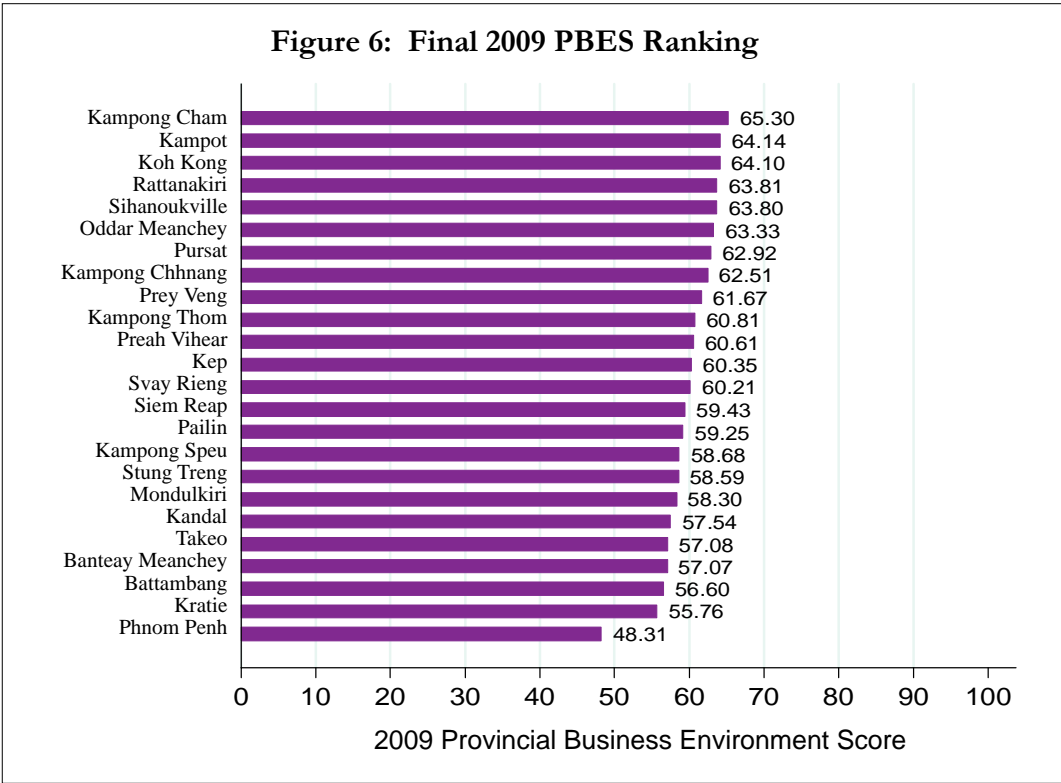
4.1 Rankings

Figure 6 presents the results of the 2009 PBES. This is the sum of provincial scores on each of the 10 sub-indices. Because 10 possible points are available for each sub-index, the final ranking is on a 100 point scale. To achieve perfection, a province would need to be ranked first in every one of the PBES indicators. It is important to

remember that the rankings are relative, based on best practices in Cambodia. Provinces are not being compared to some ideal and possibly unobtainable measures.

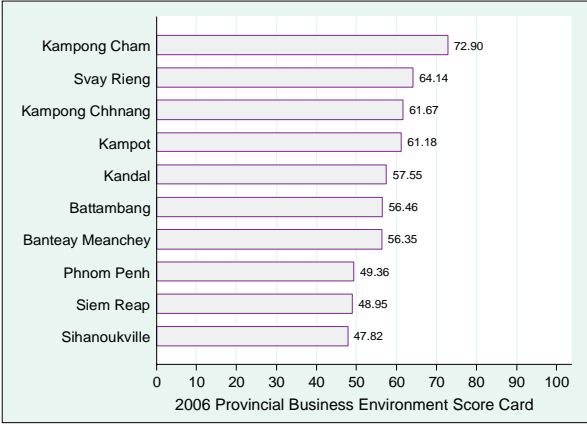
4.1.1 Kampong Cham retains top position

As in 2006, Kampong Cham is the top-ranked province, though in 2009, the gap between the provinces ranked first and second is much smaller. Kampot, the fourth-ranked province in the 2006 index, has moved up to second place. Now only two points separate Kampot from



⁹ For a detailed explanation of how the scores were compiled, see Chapter 8, Section 3 and the PBES Report 2006.

Figure 7: Final 2006 PBES Ranking



Kampong Cham; in 2006, the gap between Kampong Cham and Svay Rieng, the second ranked province, was almost 9 points. Although consistently ranking first, Kampong Cham still has aspects of economic governance that need to be improved. While provincial officials continue to earn high scores on proactivity and dispute resolution, ratings concerned with entry procedures, land access, transparency, and informal charges have declined noticeably. Sihanoukville and five newcomers (Koh Kong, Pursat, Oddar Meanchey, Rattanakiri, and Prey

Veng) complete the list of provinces that scored above 60 points. Phnom Penh, the national capital and heart of the Cambodian economy, ranks last. A margin of over six points separates it from the other low-ranking provinces.

4.1.2 The case of Phnom Penh

The extremely low score for Phnom Penh warrants special explanation. To some extent, Phnom Penh is handicapped by urbanization and population density, problems that do not burden its peers. Municipal officials in Phnom Penh are stretched to capacity in order to provide services for such an enormous population and cater to the many and complex demands of the country’s most diverse population. It is not surprising that waiting periods for business documentation and land titles take longer. There are simply not enough government officials and resources to meet the demands. In addition to a shortage of officials, urbanization poses distinct problems (crime, pollution, heavy use of infrastructure and maintenance costs). These issues pose challenges not found to the same extent in other regions. Thus, Phnom Penh’s

Testimonials about entry costs from Koh Kong Province, the highest ranked newcomer in the 2009 PBES.

Manufacturing Enterprise Manager:
I did not need to go to a government office to apply for a permit for my business. Government officials came to me, instead. It took one week to receive a Patent tax license and three days for a license from the Provincial Department of Industry, Mines and Energy.

Electric Equipment Shop Owner: A

government official came to my business with an application for a permit. It took only one week to receive a Patent tax license and one more week for a permit from the Provincial Department of Commerce.

Restaurant Owner: A Patent tax license took only one day to process after we collected and submitted all required documents from village and commune chiefs. I had to negotiate the application price as there is no official price schedule. It would be good to have one-window service to take care of business establishment paperwork.

Table 2: Comparison of Phnom Penh to Business Environments in Other Provinces

| Indicator | Phnom Penh | Other |
|---|------------|-------|
| Percentage of enterprises denying the occurrence of bribery | 45% | 68% |
| Percentage of enterprises denying commission payments on government contracts | 13% | 32% |
| Percentage of enterprises paying protection payments to local police | 30% | 5% |
| Percentage of enterprises negotiating tax payments with local officials | 67% | 57% |

low performance can be justified, in part, by its unique position as the centre for Cambodia’s economic and social life.

On the other hand, many of Phnom Penh’s sub-index scores cannot be explained only by its urban status. Interviewee responses in Phnom Penh indicate that civil servants stand out for their low level of service quality. The 2009 PBES data show that this is not matched elsewhere in Cambodia. As Table 2 shows, compared with other provinces, business owners in Phnom Penh are far more likely to: 1) pay small bribes to local officials; 2) pay commissions in order to win government contracts; 3) give protection payments to local police officers to avoid criminal activity; and 4) negotiate their tax payments with local officials.

It is little wonder that business owners in Phnom Penh appear to blame the government for their troubles (only 32% rated officials’ attitudes as positive) and many lack confidence in public institutions (only 18% believe that local institutions will protect their property rights). Worse yet, poor governance has affected the attitudes of local entrepreneurs in the capital. Whereas 60% of entrepreneurs elsewhere in the country plan to expand operations over the next two years, just 45% of businesses in the capital have such plans. In fact, 3.6% of Phnom Penh firms are planning to close down in the next two years, compared to only 1% of firms in the rest of the country.

Phnom Penh will remain the center of the Cambodian economy for the foreseeable

future. It will continue to have the largest share of business activity, as well as attract the most investment and the most talent. These successes result not from good governance, but from Phnom Penh’s endowments which include: a large urban market for goods and services; the country’s most highly educated population; far better infrastructure; cheaper energy prices; and close proximity to government and thereby to opportunities for lucrative national contracts. Nevertheless, governance in Phnom Penh will continue to constrain overall growth. Phnom Penh will never reach the full economic potential that its endowments provide unless something is done to improve service quality and reduce the risks of doing business.

**4.2 Improvement in Some Provinces’
Rankings Over Time**

Since the 2006 PBES, a number of provinces have taken important steps to improve their business environment.

The largest improvers were Sihanoukville and Siem Reap. Both ranked near the bottom in the 2006 rankings, but have since moved up to the top and middle tiers respectively. Siem Reap demonstrates improvement in nearly 9 of 10 categories. Sihanoukville has taken a less consistent path, improving radically on five subindices, despite slight declines and stagnation in others. In general, Sihanoukville’s advances outweighed its set-backs. Both provinces showed the most dramatic advances in preventing crime, facilitating entry costs, securing property rights, and enhancing transparency.

Governance Improvements in Siem Reap

A guest house owner said he finds out about new laws and regulations that affect his business from newspapers, media coverage, and respective government departments. "The provincial tax department comes four times per year to give information on tax issues," he said. "The provincial department of tourism provides information on tourist trends, rules, and regulations."

It is useful to think about the rapid governance improvements of Siem Reap and Sihanoukville in contrast to decline in the nation's capital. Like Phnom Penh, these localities benefit from propitious endowments. Siem Reap attracts tourists every year due to the unparalleled splendor of the Angkor Wat complex, while Sihanoukville receives investment because its Cambodia's only deep water port, tourism has strong potential and Sihanoukville has possible

oil reserves off its coast. Both locations could easily rest on their laurels, attracting investment every year while making minimal advances in governance and regulation. Yet, in the last two years, both locations have invested significant resources to create more efficient and transparent regulations. Siem Reap especially stands out as one of only a few provinces that have easy-to-understand regulatory information readily available in the lobbies of government agencies.

Sihanoukville also excels in transparency of business information. The research team, which visited all 24 provinces, found that Sihanoukville agencies were among a select group with regulatory information clearly posted, and where maps of future infrastructure projects were readily accessible, without having to make special requests or contacts to obtain them. By contrast, other provinces (Phnom Penh, Battambang and Banteay Meanchey) have slipped over time. These declines were primarily a result of lower scores on land access, informal charges, and tax administration.

Land Titles in Battambang

A businesswoman described her experience applying for a land title. First, she went to the village and commune offices for an application and had to make a payment for the application and for each required signature. At the tax office, she had to negotiate the tax fee. At first, tax officials wanted to collect taxes on 2.5 times the actual market price of her land.

"My land cost 10 USD per square meter on the market, but [the government officials] quoted the price at 25 USD per

square meter. I asked them to buy my land if they were sure about the price. I had to negotiate the tax price three times and pay fees for all kinds of services, including paper, pen, stamp, and even for them to complete the form. I wondered for what do they receive their government salaries? My last stop was at the Department of Land Management, Urban Planning and Construction. My application for the land title will take two to three months to process and cost \$5,000 for a 30m x 80m plot."

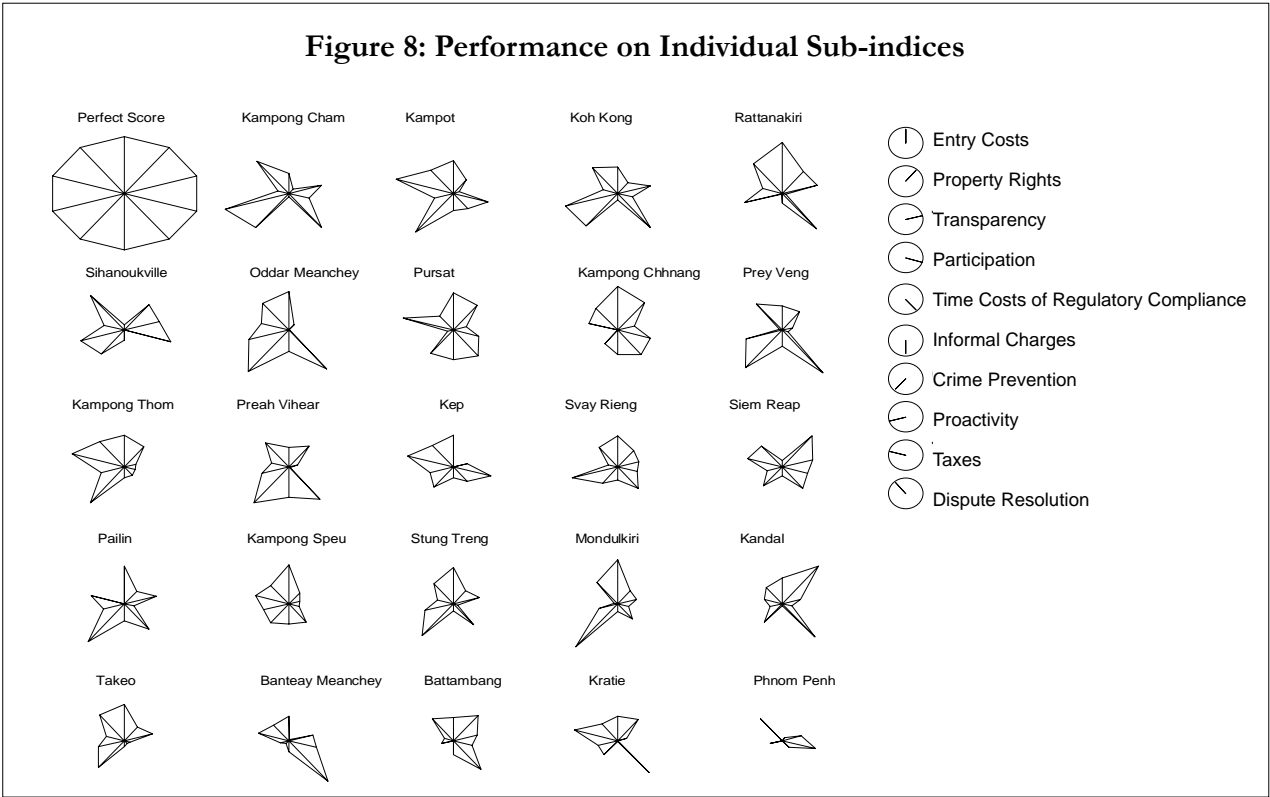
4.3 High Ranking, But Far From Perfect

In contrast to other countries, where subnational indices have been created¹⁰, Cambodian provinces are tightly clustered in their final scores. No single province stands out as having far better governance than its peers. With very little reform effort, low ranking provinces could quickly climb up the ladder in future surveys.

Even the top-ranked provinces of Kampong Cham and Kampot have much room for improvement. This fact is vividly displayed in the star charts in Figure 8, where branches represent performance on each of the individual sub-indices. An ideal province that scored a 10 on each sub-index is represented in the top left-hand corner of the figure. After

this perfect score, figures for each province are displayed according to their final PBES score. It is important to note that no province comes close to the ideal.

Furthermore, significant deficiencies are evident, even in the provinces with the very highest rankings. For instance, informal charges and tax administration continue to pose obstacles to business owners in Kampong Cham. Similarly, Kampot officials have more work to do in improving transparency and proactivity in local decision making. By contrast, lower ranked provinces have achieved success in isolated areas. Their policies for achieving these scores deserve study and emulation. As an example, Kandal (ranked 16th overall) ranks among the top provinces in terms of property rights and the time spent complying with regulations.



¹⁰ The Provincial Competitiveness Index (PCI) in Vietnam, the Economic Governance Index in Sri Lanka, and similar indexes in Indonesia or the Philippines. For more information see: <http://www.youtube.com/watch?v=7UPgFRtkm0>

4.4 Impact of Governance Improvements

By improving governance in areas where their scores are lowest, provincial officials help MSMEs to prosper. When regulation and arbitrary enforcement costs are reduced, entrepreneurs are more likely to risk their capital and energies on business expansion. A ten-point improvement in PBES scores, roughly the difference between Kratie and Kampong Cham, results in a 9.9% increase in the chance that an entrepreneur will expand his/her business. This relationship is illustrated more succinctly by the blue line in Figure 9. Appendix 3 provides the full regression results that generated this figure.

Table 3 shows that five sub-indices are of primary importance for provinces to consider improving in order to encourage entrepreneurs to expand their businesses: informal charges, ease of regulation, entry procedures, crime prevention, and tax administration. For instance, a single point improvement on the informal charges sub-index is associated with

a 3.3% increase in the chance of business expansion. Time cost of regulatory compliance, entry procedures, crime prevention, and tax administration are associated with changes of similar size. The other sub-indices are of lower priority with regard to business expansion.

Policy decisions always involve trade-offs. Devoting time, energy, and financial resources to one policy goal, generally means that other objectives are left wanting. Knowing which policy choices will provide the biggest spur to business activity can be a crucial factor in helping narrow the choice of initiatives that provincial officials should consider. Table 3 should be a useful tool for provincial authorities to use in choosing among these important policy tradeoffs. Appendix 4 provides the full regression results which generated this table.

It is, however, important to note that although participation or transparency rank very low, they may be instrumental in achieving progress in the high impact sub-indices.

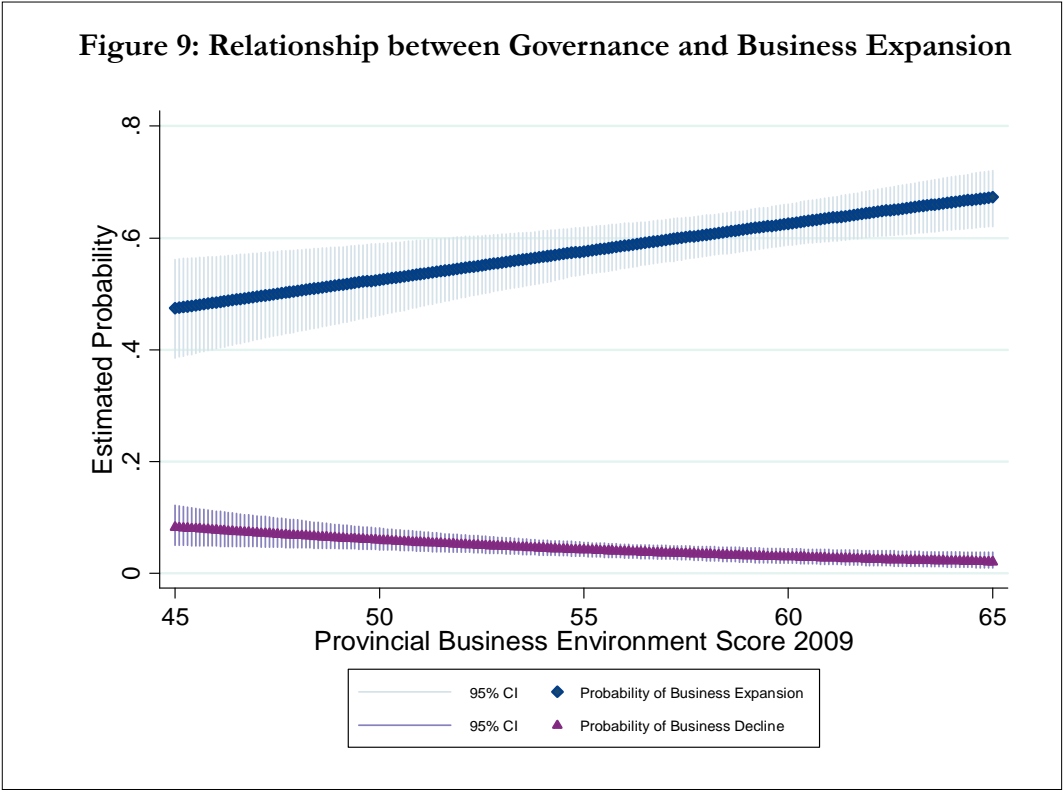


Table 3: Impact of Individual Sub-indices on the Probability that Business Owners will Expand their Businesses

| Index | Marginal Probability of Business Expansion (Based on 1-Point Increase in Sub-index) | Potential Impact |
|--|--|------------------|
| Informal Charges | 3.5%* | High |
| Time Costs of Regulatory Compliance | 3.3%* | High |
| Entry Procedures | 3.1%* | High |
| Crime Prevention | 2.7%* | Medium |
| Taxes | 2.2%* | Medium |
| Proactivity | 0.4% | Low |
| Property Rights | 0.2% | Low |
| Participation | 0.0% | Very Low |
| Transparency | -1.0% | Very Low |
| Dispute Resolution | -1.8 | Very Low |
| *Indicates that coefficient was significant at the 0.1 level or lower. | | |

4.5 Conclusions and Policy Implications

The PBES provides valuable information on how local business owners perceive and understand their business environment, what constrains them and how they feel about the performance of their public sector counterparts on different aspects of economic governance. It also highlights differences among provinces and shows that some provinces perform better than others in specific areas. It is thus a useful tool for local officials, the private sector, and other stakeholders to use in comparing the performance of their province with the performance of other provinces. This tool can also help officials to identify the specific strengths and weaknesses of their local business environment. As such, the PBES provides a practical tool for provincial officials to use in developing an actionable policy agenda and in consulting with the private sector.

In depth analysis of PBES results will help local officials and businesses to develop strategic public-private partnerships to address weak links and build on better practices. Also, even more important than comparing their overall rankings with other provinces, provinces have a great opportunity to learn from each other and share best practices and lessons learned by studying how performance on each sub-index varies from province to province.

In terms of prioritization, provincial officials may want to concentrate their learning and reform activities on reducing informal charges, crime, entry costs, regulatory enforcement costs, and the burdens of tax administration. These sub-indices are most highly correlated with prospects for business expansion. Also, mechanisms for gathering the opinions of businesses and enabling them to participate in shaping local policy generally appear to be of great importance in achieving governance improvements.

5. Sub-indices of the PBES

This section of the PBES report expands upon the concepts of economic governance discussed in Section 2 in three ways. First, we outline the motivations behind the selection of the ten sub-indices included in the PBES and detail the specific indicators used to compile these sub-indices. Second, we explain how, for each of the indicators, the raw data was converted into specific and actionable measures. Finally, we report the performance of each of the provinces on specific indicators.¹¹ This section will help officials understand how governance is understood and measured by this report, as well as their performance relative to their peers. This understanding of the PBES results will help officials design better policies to improve their local business environment and ultimately the performance of businesses in their province.

5.1 Entry Costs

Despite the initiation of a Commercial Law in 2005 and the implementation of One Window Service (OWS) for business registration in select Cambodian provinces,¹² there is still widespread frustration among small businesses in regard to the difficulties and costs of formally setting up a business. One garage owner in a northeastern province complained that he has missed out on lucrative business opportunities with international organizations, because his company is not registered and, therefore, not eligible for international contracts. While he has

a one-year operating license and pays his patent tax regularly, he has found the regulations for business registration to be opaque and confusing. So many provincial agencies have given him contradictory information that he is wary of starting the process only to find himself on the wrong side of the law. A business in Phnom Penh depicted a different aspect of the business registration process. After visiting an OWS office and discovering nobody there, he found it necessary to hire a provincial government official to handle his paperwork, paying \$650 for registration and \$400 for the official's services. In total, he paid roughly ten times the official fee for registration posted on the Ministry of Commerce website. The Investment Climate Assessment also found extensive evidence of extra charges, and deemed these to be a significant burden on the entry decisions of local entrepreneurs.¹³

The Entry Costs Sub-index draws upon widespread and extensive research which indicates that starting a business anywhere in Cambodia can be difficult, expensive and time consuming. Because business entry is complicated, we divided this sub-index into two dimensions, capturing: 1) the length of waiting periods and the number of required documents and procedures involved with starting a business; and 2) the official expense of acquiring each required document. The final results from this sub-index are shown in Figure

¹¹ Please see Appendix 1 for a detailed description of the indexing methodology.

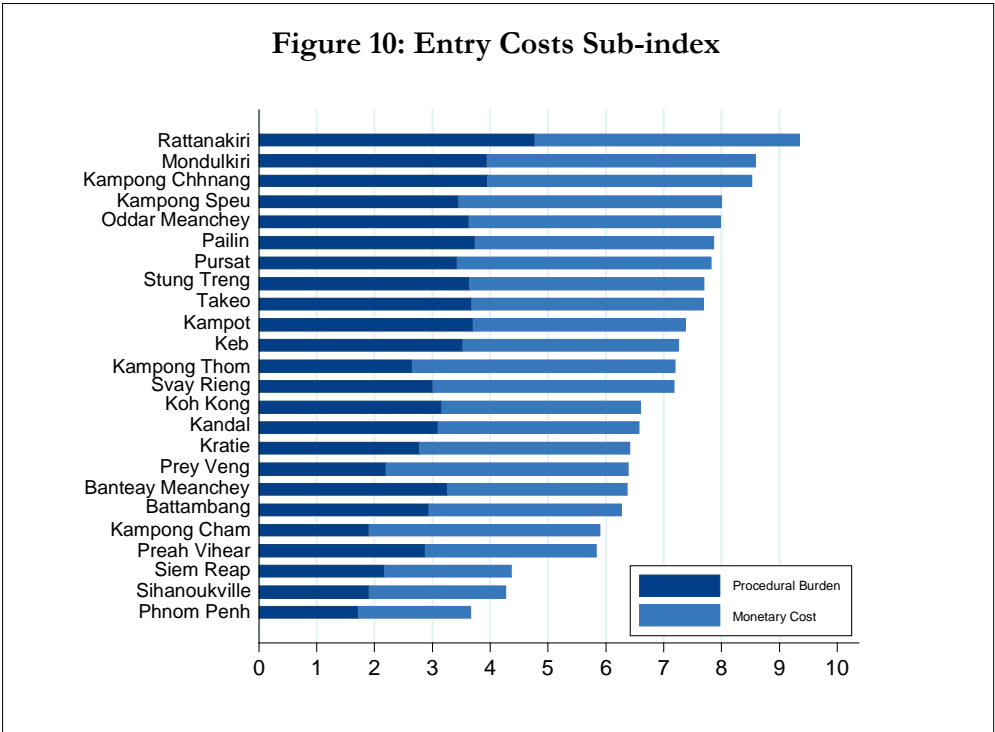
¹² World Bank and IFC. 2009: 35.

¹³ Ibid.

10 below. Answers were re-scaled, so that the shortest wait and lowest expense payments were re-coded as 10, while the most cumbersome and expensive environments received a 1.¹⁴ In other words, the best-performing provinces get the highest scores. Using our approach, the Northeastern provinces of Rattanakiri (9.34) and Mondulkiri (8.59) have the highest scores on entry costs, while Phnom Penh (3.66) has the most burdensome procedures and costs. Of the ten provinces surveyed in 2006, Kampong Chhnang ranked highest with a score of 8.59.

Developing a simple gauge of Entry Costs

in the Cambodian context is complicated by two factors. First, depending on their level of formalization, different firms confront varying start-up procedures. Using its specific methodology for limited liability companies in the national capital, the World Bank documented at least nine separate steps that an entrepreneur must complete to turn a business idea into a legal enterprise. Moreover, the official fees required to start a business were calculated to be 152% of per capita income, which is over nine times more expensive than in neighboring Vietnam and places Cambodia’s business entry costs at 169th out of 181 economies in the world.¹⁵



¹⁴ Re-scaling uses the following formula, in which Province_i is the individual provincial value, minimum is the smallest provincial value in the sample, and maximum is the largest provincial value in the sample.

$$9 * \left[\frac{\text{Province}_i + \text{Minimum}}{\text{Maximum} - \text{Minimum}} \right] + 1$$

For some calculations, a large number has a negative interpretation. In these cases, we reverse the index by subtracting the entire quantity from 11.

$$11 - 9 * \left[\frac{\text{Province}_i + \text{Minimum}}{\text{Maximum} - \text{Minimum}} \right] + 1$$

¹⁵ World Bank. 2009. *Doing Business 2009*. (<http://www.doingbusiness.org/>)

However, most firms in Cambodia do not meet the rigid criteria used in the World Bank’s *Doing Business* report. Indeed, only 38 of the 1234 firms in our sample (3.1%) had a registration certificate from the Ministry of Commerce, and almost 936 (or 76%) lacked the common one-year provincial certificate that is often issued in lieu of full registration but that does not establish clear legal authority. When asked both in focus groups and the survey why they have not registered, most firms cited their small size, unnecessary registration costs, and a fear that registration would invite unwanted attention from the tax authorities.

Table 4 summarizes the five levels of formalization identifiable in the Cambodian business context: 1) Fully Formal – National Level; 2) Fully Formal – Provincial Level; 3) Unregistered with Operating License; 4) Possession of Patent Tax; and 5) Fully Informal. Because each of the five levels involves different interactions with provincial authorities and varying waiting periods, it was important that the Entry Costs Sub-index incorporate these nuances by considering the opportunity costs of detailed procedures on businesses while not penalizing provinces for implementing national laws that require documentation.

Table 4: Levels of Cambodian Business Formalization

| Level | Description | Key Documents Required | Representation in PBES Samples | |
|-------|--|---|--------------------------------|----------------------------|
| | | | 2009 Full | 2009 Original 10 Provinces |
| 1 | <i>Fully Formal – National</i> | Registration at Ministry of Commerce; Three-year Operating License from relevant ministry†; Patent Tax registration at National Tax Authority; Value Added Tax (VAT) identification number from Ministry of Economics and Finance; Paying profit tax under real tax regime; Labor permit certifying approval of company’s internal rules for enterprise with over 8 employees; Environmental Certificate governing solid waste and water disposal from the Ministry of Environment; Other licenses when applicable‡ | 4.3% | 5.5% |
| 2 | <i>Fully Formal – Provincial</i> | License to Operate Commercial Enterprises from Provincial/Municipal Department of Commerce*; One-Year Operating License from Ministerial Department at Provincial Level†; Patent Tax registration at Provincial/Municipal Tax Authority; Paying estimated tax if under \$1500 annual profits; Other licenses including Labor Permit and Environmental Certificate when applicable‡ | 22.1% | 21.5% |
| 3 | <i>Unregistered w/ Operating License</i> | One-Year Operating License from Ministerial Department at Provincial Level†; Patent Tax registration at Provincial/Municipal Tax Authority; Other licenses including Labor Permit and Environmental Certificate when applicable‡ | 13.3% | 14.3% |
| 4 | <i>Patent Tax</i> | Patent Tax registration at Provincial/Municipal Tax Authority | 23.7% | 19.6% |
| 5 | <i>Fully Informal</i> | No formal documentation | 35.7% | 40.3% |

† The 4 most common are the Factory Operating License for Industrial Enterprises from the Heavy Industries Section of MIME; Handicraft Operating License from Handicraft and Light Industries Section of MIME; the Service Sector Operating License from MOT; and the Agricultural, Forestry, and Fisheries Operating License from the Ministry of Agriculture, Forestry, and Fisheries.

‡ These include Construction Permits from the Ministry of Land Management, Urban Planning, and Construction, Road Construction License from the Ministry of Public Works, Sanitation Permits, and Import/Export Licenses from the Customs Authority.

Ψ The Patent tax is an annual registration (or license) fee levied on *all businesses*, industries and professions, though farmers are exempted. The tax is based on turnover from the previous year. New businesses must register with the tax authorities within 15 days after economic activity (Law of Taxation, 1999). The first Patent tax is estimated in accordance with the performance of similar enterprises. Firms that don’t wish to export may register with provincial-municipal commerce division (under *Prakas 78-MOC-2002*).

* Firms that don’t wish to export and are not eligible to pay profit taxes under the “real regime,” as they have below \$1500 in annual profits (Article 12 of Law on Commercial Enterprises and Registration) and not eligible may register with the Provincial/Municipal Commerce Division according to *Prakas 78-MOC-2002*, but they are not considered a legal entities. Firms that don’t wish to export may register with provincial-municipal commerce division (under *Prakas 78-MOC-2002*). Firms that don’t wish to export may register with provincial-municipal commerce division (under *Prakas 78-MOC-2002*). Firms that don’t wish to export may register with provincial-municipal commerce division (under *Prakas 78-MOC-2002*).

A second obstacle to proper measurement of Entry Costs is that many firms do not actually experience these bureaucratic waiting periods directly. In the PBES sample, 24% of the firms hired facilitators to handle business registration activities on their behalf. In 40.3% of cases, the facilitator was an employee of a provincial government agency; other firms hired family members or individuals who did not work for the government. Because facilitators took care of all paperwork, these enterprises could not always answer detailed questions about the waiting periods or about the official costs of obtaining documents.

Consequently, firms that used facilitators were asked only whether they possessed specific documentation. They were not invited to answer detailed questions about the cost of business registration activities.

5.1.1 Waiting Periods and Procedures

The Waiting Periods Dimension is a composite measure of the time burden involved for a firm to become a legal enterprise. It consists of five different measures, each one re-scaled to 10 points.

1. *Percentage of fully formal enterprises (national or provincial)*
2. *Percentage of firms in the province requiring less than five formal documents (including all registrations, licenses, and permits) to start their business*
3. *Median waiting period for Registration Certificate from the Provincial/Municipal Department of Commerce.*
4. *Median waiting period for a One-Year Operating License from the relevant provincial department for a firm's products or services.*
5. *Median waiting period for Patent Tax registration from Provincial or Municipal Tax Authority.*

The first two measures are explained below:

- *The percentage of fully formal enterprises (national or provincial)* is the first measure of procedural costs. The key assumption of this indicator is that if more firms have taken all necessary steps to become fully legal, then the provincial administration can be considered more encouraging toward formalization and ensuring the ease of procedures. Before using this indicator, diagnostic checks by the research team confirmed that variation in registration was not determined by differences in the average size of businesses or manufacturing firms at the provincial level – rather, the measure is primarily an indicator of bureaucratic procedures.¹⁶

To further indicate that registration is not based on the sophistication level of businesses, two of the highest proportions of registered firms were surprisingly in Northeast Cambodia (Rattanakiri 65% and Stung Treng 60%), where firms are particularly small. Only twenty percent of operations in Rattanakiri and 7.5% in Stung Treng have over 6 employees. Concerned about the validity of the data, the research team called every registered firm in these provinces to ask them if they truly possessed valid documentation. It turned out that all had them and indicated that, unlike in other provinces, officials from the Department of Commerce actually made special trips out to their business location to visit them and enroll them directly. They did not initiate the registration procedures themselves. This procedure is obviously easier to manage in rural areas with limited numbers of enterprises than in more economically active provinces such as Phnom Penh.

- *The percentage of firms in the province requiring less than five formal documents (including all registrations, licenses, and permits) to start their business.* This

¹⁶ Bivariate Correlations with the percentage of fully formal firms are: 0.27 with the provincial average of total assets; 0.44 with employment size, and -0.04 with the percentage of manufacturing firms.

measure captures the number of bureaucratic steps that are required for a firm to be fully legal in each province. Most firms in the PBES survey actually needed to complete only a few steps. Though fully formal enterprises required slightly more documentation, the burden imposed by the number of procedures they needed to complete was still not that large. Ten point three percent of fully formal enterprises needed more

than five documents, as opposed to only 1.5% of those at lower levels of formalization.

The other three indicators measure the median waiting period required to obtain the three most common types of firm documentation. Only firms that had completed the necessary procedures themselves and possessed the actual document were eligible to answer the questions.

Table 5: Indicators Comprising Entry Costs (Dimension 1)
Waiting Periods/Procedures

| Province | Fully formal firms (%) | Firms requiring less than 5 legal documents (%) | Wait for Provincial Registration Certificate (Median Days) | Wait for Provincial Operating License (Median Days) | Wait for Patent Tax Certificate (Median Days) | Dimension 1 Score* |
|--|------------------------|---|--|---|---|--------------------|
| Rattanakiri | 65.0% | 2.5% | 2 | 3 | 2.5 | 4.77 |
| Kampong Chhnang | 35.8% | 1.9% | 18.5 | 7 | 7 | 3.96 |
| Mondulkiri | 37.5% | 2.5% | 5 | 11 | 7 | 3.95 |
| Pailin | 12.5% | 2.5% | 7 | 7 | 5.5 | 3.75 |
| Kampot | 42.3% | 3.8% | 15 | 14 | 7 | 3.71 |
| Takeo | 22.5% | 2.5% | 10 | 11 | 7 | 3.68 |
| Stung Treng | 60.0% | 7.5% | 15 | 15 | 7 | 3.65 |
| Oddar Meanchey | 15.0% | 0.0% | 10 | 7 | 15 | 3.63 |
| Keb | 22.5% | 7.5% | 15 | 2 | 7 | 3.53 |
| Kampong Speu | 30.0% | 2.5% | 30 | 15 | 7 | 3.45 |
| Pursat | 17.5% | 5.0% | 15 | 12.5 | 3.5 | 3.43 |
| Banteay Meanchey | 1.9% | 3.8% | 15 | 10 | 7 | 3.26 |
| Koh Kong | 20.0% | 0.0% | 30 | 10 | 22.5 | 3.16 |
| Kandal | 32.7% | 11.5% | 15 | 7 | 10 | 3.10 |
| Svay Rieng | 25.0% | 3.8% | 8.5 | 30 | 7 | 3.02 |
| Battambang | 25.9% | 3.5% | 25 | 20 | 15 | 2.94 |
| Preah Vihear | 12.5% | 0.0% | 30 | 18 | 20 | 2.88 |
| Kratie | 10.0% | 5.0% | 2 | 30 | 7 | 2.78 |
| Kampong Thom | 40.0% | 5.0% | 30 | 30 | 15 | 2.66 |
| Prey Veng | 5.1% | 0.0% | 90 | | 22.5 | 2.21 |
| Siem Reap | 29.9% | 8.0% | 15 | 22.5 | 30 | 2.18 |
| Sihanoukville | 57.7% | 11.5% | 30 | 30 | 30 | 1.91 |
| Kampong Cham | 15.4% | 3.8% | 30 | 30 | 30 | 1.91 |
| Phnom Penh | 21.0% | 8.7% | 30 | 26.5 | 30 | 1.72 |
| Prey Veng did not have enough firms with operating licenses to generate statistically reliable results Scores are re-scaled between .6 (1*.6) and 6 (10*.6), as this dimension represents 60% of the 10-Point sub-index | | | | | | |

5.1.2 Monetary Costs of Business Entry

This is a composite measure of the official costs required for a firm to become a fully legal enterprise. The Money Dimension consists of five different measures, each one re-scaled to 10 points:

1. *Median cost ("official fee") for Registration Certificate from the Provincial/Municipal Department of Commerce.*
2. *Median cost ("official fee") for One-Year Operating License for firm products or services from relevant provincial departments.*
3. *Median cost ("official fee") for Patent Tax registration from Provincial or Municipal Tax Authority.*
4. *Percentage of provincial revenue derived from processing Patent Tax registration.*
5. *Percentage of provincial revenue derived from enterprise registration and stamps processing.*

The first three indicators measured the median costs charged to firms for obtaining the three most common types of firm documentation. As mentioned above, only firms that had completed the procedures themselves and possessed the actual document were eligible to answer the questions. Though the research team labeled these indicators as "official" costs, this is a euphemism. Although the registration fees are set by regulations at the national level that does

not allow for provincial variation, in reality the variation is quite high. The median fees charged to firms varied from \$5 in Svay Rieng to \$50 in Preah Vihear. Thus, "official" fees almost certainly include additional informal charges levied by provincial officials, taking advantage of the lack of information. When the PBES research team asked provincial officials for verification of the official fees cited by firms, they were unable to provide the information.

Official fees for firms' legal documents were never meant to be a primary source of revenue for provincial administrations. Instead, they were intended to reflect the labor and material costs of processing such documentation. Nevertheless, according to provincial budget information, these fees comprise a significant portion of revenue in some provinces – ranging from a total of 0.13% in Preah Vihear to 34.7% in Kandal. The heavy reliance of provincial administrations on processing fees for revenue is a clear indication that firms are over-paying to formalize and subsidizing a portion of provincial services. Consequently, the last two measures derived from provincial budgets, *the percentage of provincial revenue derived from processing Patent Tax registration and the percentage of provincial revenue derived from enterprise registration and stamps processing* offer a useful complement to official fees in the Money Dimension of the Entry Costs Sub-index.

Table 6: Indicators Comprising Entry Costs (Dimension 2)
Official Fees

| Province | Official fee for Provincial Registration Certificate (Median \$) | Official fee for Provincial Operating License (Median \$) | Official fee for Patent Tax Certificate (Median \$) | Revenue derived from processing Patent Tax Certificate (%) | Revenue derived from enterprise registration and stamps processing (%) | Dimension 2 Score* |
|--|--|---|---|--|--|--------------------|
| Mondulkiri | 10 | 8 | 10 | 0.19% | 0.19% | 4.64 |
| Rattanakiri | 10 | 10 | 10 | 0.22% | 0.56% | 4.57 |
| Kampong Chhnang | 6.5 | 9 | 10 | 1.30% | 1.41% | 4.57 |
| Kampong Speu | 8 | 8.5 | 6 | 5.58% | 2.33% | 4.55 |
| Kampong Thom | 15 | 10 | 7 | 0.23% | 1.46% | 4.54 |
| Pursat | 25 | 11 | 5 | 0.82% | 1.45% | 4.39 |
| Oddar Meanchey | 7.5 | 12 | 15 | 0.61% | 0.55% | 4.35 |
| Prey Veng | NA | NA | 10 | 0.42% | 2.77% | 4.19 |
| Svay Rieng | 5 | 6.5 | 7.5 | 20.12% | 2.89% | 4.16 |
| Pailin | 25 | 15 | 10 | 2.27% | 0.47% | 4.12 |
| Stung Treng | 15 | 20 | 15 | 0.19% | 0.45% | 4.05 |
| Takeo | 10 | 31.5 | 7.5 | 1.14% | 3.26% | 4.01 |
| Kampong Cham | 20 | 11 | 10 | 3.18% | 4.12% | 4.00 |
| Kep | 22.5 | 16 | 20 | 1.34% | 0.38% | 3.73 |
| Kampot | 17.5 | 30 | 13 | 3.77% | 2.13% | 3.66 |
| Kratie | 8 | 50 | 10 | 1.04% | 2.19% | 3.64 |
| Kandal | 10 | 10 | 10 | 34.71% | 3.12% | 3.48 |
| Koh Kong | 30 | 22.5 | 15 | 6.17% | 1.83% | 3.44 |
| Battambang | 17.5 | 17 | 15 | 15.69% | 4.71% | 3.33 |
| Banteay Meanchey | 13 | 40 | 17.5 | 5.03% | 4.69% | 3.11 |
| Preah Vihear | 50 | 25 | 21.5 | 0.13% | 0.40% | 2.96 |
| Sihanoukville | 42.5 | 20 | 20 | 22.66% | 4.78% | 2.36 |
| Siem Reap | 15 | 15 | 25 | 24.46% | 11.88% | 2.19 |
| Phnom Penh | 30 | 30 | 22.5 | 30.86% | 6.48% | 1.94 |
| Prey Veng did not have enough firms with operating licenses to generate statistically reliable results. | | | | | | |
| Scores are re-scaled between .4 (1*.4) and 4 (10*.4), as this dimension represents 40% of the 10-Point sub-index | | | | | | |

5.2 Property Rights

Hernando de Soto, a Peruvian economist, demonstrated the importance of land titles in economic development by pointing out that legal property rights encourage investment in fixed assets and that, by allowing the use of title land as collateral, access to capital markets is enhanced. Galiani and Schargrodsky have tested this claim in a natural experiment in Argentina,

finding tremendous evidence that land title influences greater investment in local household property and business, as well as other forms of entrepreneurial behavior.¹⁷ They found little evidence, however, that land titles improve access to bank credit.

Recent research on Cambodia has demonstrated that formal property rights still remain relatively weak due to limited land ownership and titling.

¹⁷ De Soto. 2000, Galiani and Schargrodsky. 2007.

The Land Law of 2001 developed a legal regime for property rights and laid forth a plan for systematic land registration, which our data indicates has progressed admirably – 49% of the firms in our samples possess full titles. Nevertheless, in many provinces implementation of these procedures has barely commenced, and in those where it has, titling varies greatly. According to a baseline survey performed by Cambodian Development Resources Institute (CDRI) in 2007, 62.7% of agricultural land plots have never been documented with any kind of property rights declaration. Of the plots that do have some sort of documentation, 61.6% have receipts for certificate applications, and 14.9% have land survey investigation papers, only 8.1% have official certificates or titles.¹⁸

Since that baseline analysis, the Land Management and Administration Project has moved to actively title land in eleven Cambodian provinces. According to their figures, over one million titles were distributed between the beginning of the project and June 2009. In fact, 185,000 systematic land titles were issued in 2008 alone in the target provinces.

The widespread push on land titling between the two years of the PBES survey gives an excellent opportunity to evaluate the effectiveness of the program for private sector business development. How has expanded property rights protection influenced entrepreneurial decisions and access to capital? We deal with this more systematically in our analysis of the PBES panel survey (Section 7 of the report), but in this section we describe the provincial aggregates from the 2009 PBES.

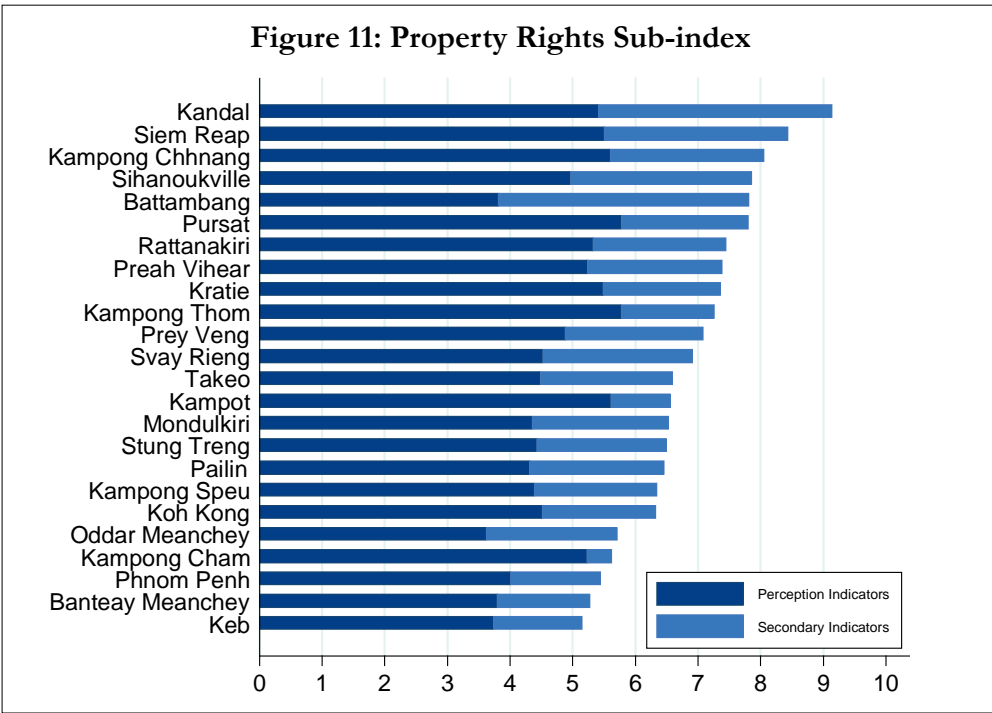
Interestingly, the 2009 World Bank's Investment Climate Assessment (ICA) found that only 10% of business operations viewed access to land as a constraint on their businesses. Though they acknowledge, that this number has risen from 3% in 2006, they attribute the low incidence in both surveys to the limited number of businesses owning the land on which they operate. According to ICA data only 36% of businesses own their own land and 39% own their own buildings.¹⁹

The PBES 2009 sample, which includes smaller and more rural enterprises, found that land ownership remains high, with 61% of firms operating on household or purchased land. In face-to-face interviews, we also found extensive evidence that land was seen as a constraint to business expansion. In two cases in Kandal and Kratie provinces, disputes over the demarcation of land with powerful officials were distracting for businesses and held up their expansion plans. In another case in Strung Treng province, an entrepreneur found the \$1,000 for administrative fees and land taxes to be a significant obstacle, as it was quite large relative to her business' monthly revenue. Firms in richer provinces like Kandal, however, thought \$1,000 was reasonable and were happy that the title was issued so quickly, often within two-months of the application.

Figure 11 demonstrates that Kandal and Siem Reap are the leading provinces in terms of safeguarding general property rights, while Phnom Penh, Banteay Meanchey, and Kep lag furthest behind. Siem Reap's rise to the top of this list has been quite remarkable. In just a few short years, it has ascended from the bottom to the top of the ranking.

¹⁸ CDRI. 2007:5

¹⁹ World Bank and IFC. 2009: 34.



5.2.1 Soft (Perceptions) Data

Five indicators are used to generate the survey-based Dimension 1:

1. *Percentage of provincial firms with any documentation regarding the ownership of purchased or household land.*
2. *Percentage of firms with Solid Titles and Pre-2000 Title.*
3. *Percentage of firms that consider expropriation by provincial officials to be a frequent or constant risk.*
4. *Percentage of firms that consider the risk of changes in rental contracts is high or very high.*

• *Percentage of provincial firms with any documentation regarding the ownership of purchased or household land.* As with formal business registration, the definition of land titles is quite complicated; it involves four different levels of formality that are roughly equal to the security of property rights offered by proper land titles. For the first indicator, we take the percentage of firms in each province that have any type of documentation

related to their land. In the PBES sample, 89.24% of firms operating on purchased or household land have some documentation, but figures vary regionally, from 100% in Kandal and Pailin to 77.8% in Monduliri.

• *Percentage of firms with Solid Titles and Pre-2000 Titles.* As indicated in Table 7, Solid Titles and Pre-2000 Titles offer far more security than a soft title. For that reason, we also calculate the percentage of firms in each province that have these documents. Simply using Solid Titles would have been preferable, but there was confusion over which documents firms actually possessed, with some firms claiming they had acquired Pre-2000 titles after the year 2000.²⁰ Fifty-seven point five percent of the firms from our sample declared they had Solid or Pre-2000 Titles. The systematic land registration put forth in the 2001 Land Law is apparently having some effect.

The highest possession of Solid Titles was found in Sihanoukville and Kampong Thom.

²⁰ In June 2009, we returned to 131 firms in the panel analysis to perform a disaggregated analysis of land title possession. These results are discussed in Section 6 of this volume.

Table 7: Levels of Cambodian Land Titling

| Level | Description | Key Documents Required | Representation in PBES Samples | |
|-------|-----------------------|--|--------------------------------|------------------|
| | | | 2009 Full | 2009 Original 10 |
| 1 | <i>Solid Title</i> | Full land title issued as a result of the procedures put forth in the 2001 Land Law, which allows for all transactions including exchange and mortgage. Generally issued by Provincial or District Land Authorities, but more recently by national officials performing systematic land registration in accordance with the 2001 Law. Roughly ¼ of firms with solid titles in the PBES received their title through systematic registration. | 32.8% | 33.3% |
| 2 | <i>Pre-2000 Title</i> | A land ownership certificate issued by district authorities at a very low fee without the Solid Title's requirement for investigation of ownership or public announcement. Many firms were issued these titles before 2000. Their authenticity remains in dispute with banks and potential purchasers taking large risks that holders are the legitimate owner. Under the new law, these documents should be converted to solid titles. | 24.7% | 26.5% |
| 3 | <i>Soft Title</i> | Not an official certificate at all, but in fact the receipt for beginning the process of registration. Because land titling has often taken so long, many firms simply began trading these certificates. While they are sometimes accepted in transactions, they do not offer formal security over property. | 31.7% | 32.0% |
| 4 | <i>No Title</i> | No documentation at all. | 10.8% | 8.1% |

• *Percentage of firms that consider expropriation by provincial officials to be a frequent or constant risk.* Possession of a land title does not appear to be enough to avoid land dispute or illegal land seizure.²¹ In the past, such seizures have occurred regularly, with little or no compensation offered to local entrepreneurs. Recent media coverage has highlighted a number of disputes involving what entrepreneurs have deemed to be unfair or illegal land seizures. Entrepreneurs in our face-to-face interviews discussed similar incidences, blaming the problems on the lack of transparency of land laws and regulations. The PBES survey, however, revealed very little perception of expropriation risk. In most provinces, less than 5% of entrepreneurs indicated severe risk; in Pailin and Oddar Meanchey, where the risk is perceived as highest, one-third of firms perceived expropriation as a problem.

For 489 firms (39% of the PBES sample), the majority of business operations occur on land that is leased or rented from another party. For these firms, property rights have less to do with land titling than with their ability to operate and plan future investments without the fear

that rental arrangement changes can materially affect their business. Damaging contractual changes may include rental increases, sales to new parties, new contractual terms that limit business activity, and higher fees for property-related services. For firms that rent and lease land, we developed a further indicator of property rights.

• *Percentage of firms that consider the risk of changes in rental contracts is high or very high.* This question was designed to complement the expropriation question above for firms that rent property. Along with expropriation risk, it serves as a good indicator of entrepreneurs' belief that they will be able to hold on to their property long enough to recoup their investments.

Table 8 summarizes individual provincial scores and the final Property Rights Perception Dimension. According to firms in this PBES survey, Kampong Thom and Pursat (6.03 both) are perceived to have the strongest property rights. Rights are considered weakest in Kep (3.97) and Oddar Meanchey (3.87).

²¹ Megleng and Becker. 2009; Soenthrith 2009.

Table 8: Indicators Comprising Property Rights (Dimension 1)
Perceptions

| Province | Firms with any documentation for household or business land (%) | Firms with Solid Land/Pre-2000 Titles (%) | Firms that consider expropriation is often or always a risk (%) | Firms that consider risk of material change in rental contracts is high or very high (%) | Dimension 1 Score* |
|--|---|---|---|--|--------------------|
| Kampong Thom | 100.0% | 86.21% | 0.00% | 9.09% | 6.03 |
| Pursat | 100.0% | 50.00% | 0.00% | 9.09% | 6.03 |
| Kampot | 97.0% | 84.85% | 3.33% | 5.56% | 5.86 |
| Kampong Chhnang | 97.4% | 46.15% | 2.70% | 7.14% | 5.86 |
| Siem Reap | 100.0% | 69.57% | 0.00% | 17.46% | 5.75 |
| Kratie | 96.2% | 57.69% | 4.00% | 7.14% | 5.74 |
| Kandal | 100.0% | 74.07% | 0.00% | 20.00% | 5.67 |
| Rattanakiri | 100.0% | 72.22% | 0.00% | 22.73% | 5.58 |
| Preah Vihear | 92.0% | 48.00% | 0.00% | 13.33% | 5.49 |
| Kampong Cham | 97.0% | 69.70% | 0.00% | 21.05% | 5.48 |
| Sihanoukville | 95.5% | 95.45% | 5.00% | 20.69% | 5.21 |
| Prey Veng | 81.3% | 50.00% | 6.67% | 0.00% | 5.12 |
| Svay Rieng | 95.0% | 42.50% | 2.56% | 36.36% | 4.77 |
| Koh Kong | 84.6% | 57.69% | 8.00% | 14.29% | 4.76 |
| Takeo | 82.1% | 67.86% | 3.70% | 16.67% | 4.73 |
| Stung Treng | 92.0% | 56.00% | 9.09% | 26.67% | 4.68 |
| Kampong Speu | 82.8% | 62.07% | 0.00% | 25.00% | 4.64 |
| Mondulkiri | 77.8% | 18.52% | 9.09% | 7.69% | 4.59 |
| Pailin | 100.0% | 58.33% | 33.33% | 12.50% | 4.57 |
| Phnom Penh | 86.4% | 68.18% | 9.09% | 31.08% | 4.25 |
| Battambang | 86.4% | 44.07% | 6.00% | 40.74% | 4.06 |
| Banteay Meanchey | 79.5% | 35.90% | 8.00% | 28.57% | 4.03 |
| Kep | 57.9% | 42.11% | 6.06% | 0.00% | 3.97 |
| Oddar Meanchey | 88.9% | 51.85% | 33.33% | 16.67% | 3.87 |
| Scores are re-scaled between .6 (1*.6) and 6 (10*.6), as this dimension represents 60% of the 10-Point sub-index | | | | | |

5.2.2 Hard Data

Dimension 2 is based on a hard data proxy for the perception-based data on property rights.

Effective price of land in the province: High land prices, which are predominantly determined by the demand for and supply of available land in a particular area, limit the ability of entrepreneurs to purchase enough property to meet their expansion plans. A strong demand for business premises can also drive property values up further, particularly when useful land is scarce. A regression model that controls for supply and

demand can provide us with a residual that is the effective price of land.

More specifically, the residual is the difference between the predicted price of land (from structural conditions) and its actual price. Firms with negative residuals have under-priced land, while firms with positive residuals have land that is more expensive than what structural determinants would predict.

What is left is the part of the land price that is affected by government policy, especially by extra costs related to obtaining titles, the

transparency of land registries, and information regarding zoning policies. As one Phnom Penh firm commented, “If a title is urgently needed, a firm has to provide money to government staff to get the title on time.” Some focus group participants estimated that these extra costs could be as high as \$1,000. As the land market boomed and Cambodian real estate increased in value, the rise in the effective price for land priced many entrepreneurs out of business expansion.

Table 9 presents the results from this regression, in which the team controlled for the number of firms competing for scarce land, surface area in square kilometers, and the GDP per capita of the province. Although in theory more controls could have been employed, limited degrees of freedom prevented their use in this analysis.

of land. All told, the three variables explain about 95% of variance in the price of land. The unexplained 5% of the variance is caused by other factors captured in the residual land price.

Figure 12 demonstrates how the effective price is calculated, by plotting the estimated price per land based on the above regression on the x-axis and the residual price on the y-axis. To aid analysis, a 0 residual line is plotted in purple, meaning supply and demand conditions perfectly predict land price. Provinces with negative scores have undervalued land because of demand conditions, while provinces with positive scores tend to have prices that are higher than what would be predicted, due to demand and supply conditions. Provinces with the largest positive and negative residuals

Table 9: Regression Determination of Effective Land Price

| Independent Variables | Coefficient |
|--|----------------------|
| Number of Enterprises in Province | 0.103*** (0.0112) |
| GDP per Capita | 45.38** (21.17) |
| Surface Are in Square Kilometers | 0.00208 (0.00642) |
| Constant | -247.7*** (86.65) |
| Observations | 24 |
| R-squared | 0.955 |
| Dependent Variable: Price of M2 of Land; Robust standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1 | |

In short, Table 9 shows that land price is significantly related to the number of firms and average wealth in the province. As this is an ordinary least squares (OLS) analysis, coefficients can be read directly from the table. For instance, every 1 firm in the province collectively adds about \$1 to the predicted price

are plotted on the graphic. Land appears to be most egregiously overvalued in Kampong Cham, with prices about \$322 per square meter higher than one would predict given supply and demand conditions. They are about \$361 and \$310 undervalued in Battambang and Kandal respectively.

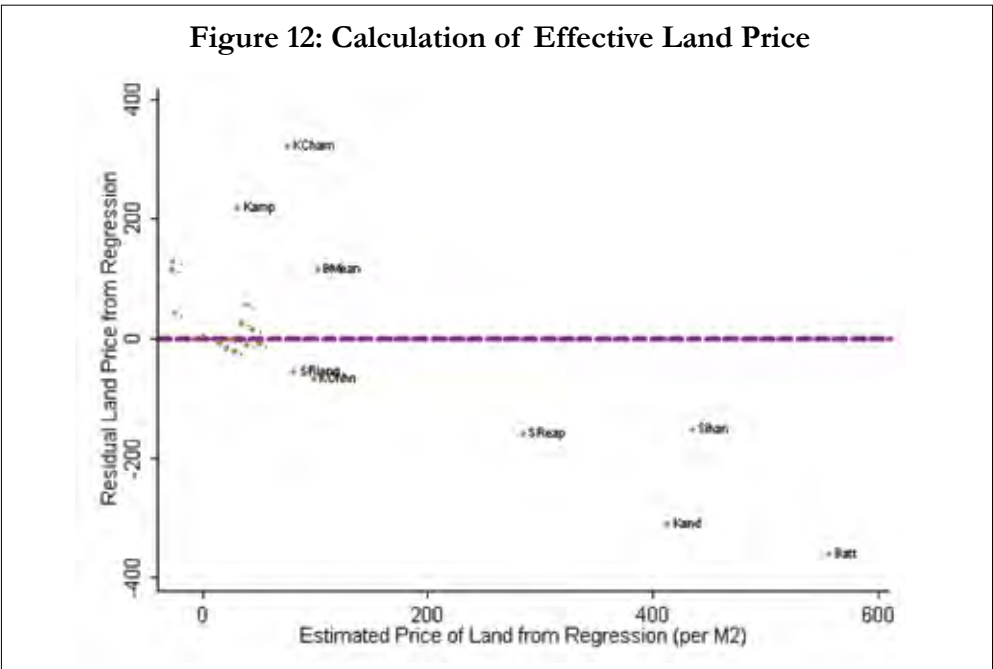


Table 10: Indicators Comprising Property Rights (Dimension 2)
Hard Data

| Province | Effective Price of Land per Meter Squared (Residual from Regression Analysis Controlling for Demand, Supply, and Structural Conditions) | Dimension 2 Score* |
|------------------|---|--------------------|
| Battambang | -361.71 | 4.00 |
| Kandal | -310.15 | 3.73 |
| Siem Reap | -159.62 | 2.94 |
| Sihanoukville | -152.64 | 2.90 |
| Kampong Chhnang | -67.31 | 2.45 |
| Svay Rieng | -55.31 | 2.39 |
| Prey Veng | -22.19 | 2.21 |
| Mondulkiri | -16.48 | 2.18 |
| Pailin | -9.20 | 2.14 |
| Preah Vihear | -8.48 | 2.14 |
| Rattanakiri | -6.73 | 2.13 |
| Oddar Meanchey | -0.01 | 2.10 |
| Takeo | 0.02 | 2.10 |
| Stung Treng | 4.39 | 2.07 |
| Pursat | 14.67 | 2.02 |
| Kampong Speu | 27.24 | 1.95 |
| Kratie | 42.89 | 1.87 |
| Koh Kong | 55.52 | 1.80 |
| Banteay Meanchey | 115.29 | 1.49 |
| Kampong Thom | 115.65 | 1.49 |
| Phnom Penh | 123.87 | 1.44 |
| Kep | 129.18 | 1.42 |
| Kampot | 218.95 | 0.94 |
| Kampong Cham | 322.13 | 0.40 |

Scores are re-scaled between .4 (1*.4) and 4 (10*.4), as this dimension represents 40% of the 10-Point sub-index

5.3 Transparency

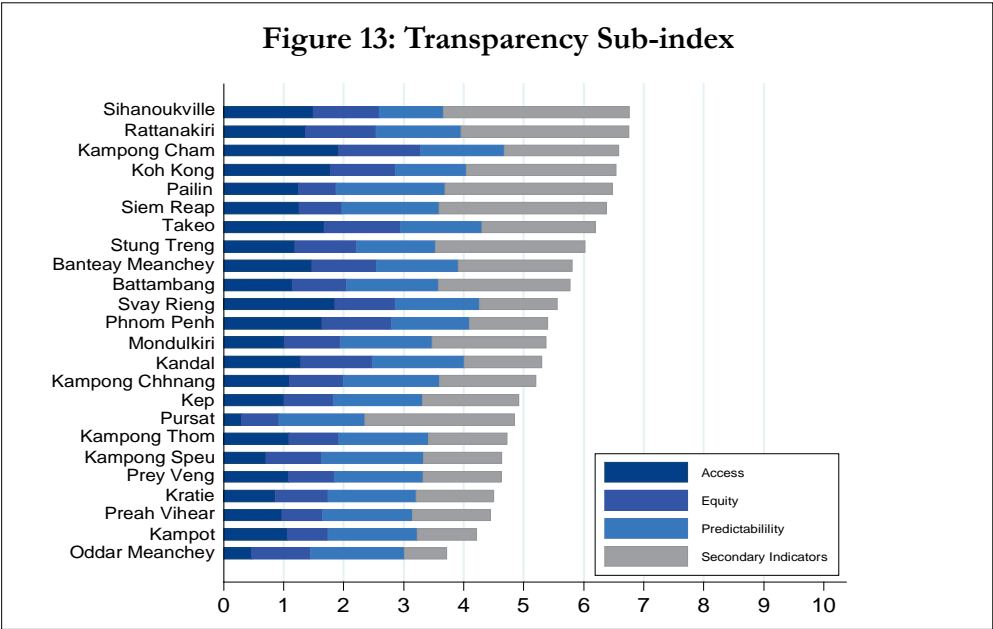
Transparency is highlighted by academics and development practitioners as one of the most crucial factors in determining the conductivity of different environments are to private business performance.²² Economists Tara Vishwanath and Daniel Kaufman (1999) define transparency as: The increased flow of timely and reliable economic, social and political information about government service provision, monetary and fiscal policy. On the other hand, a lack of transparency may be described as someone deliberately withholding access to, or misrepresenting, information or failure to ensure that the information provided is of adequate relevance and quality.

In many Cambodian provinces, basic business information can be very difficult to come by. Entrepreneurs are forced to rely on personal relationships or spend a great deal of money in order to acquire enough information to engage in rudimentary long-term planning. As a result, lack of transparency can have a pernicious effect on long-term investment, because

entrepreneurs are unable to calculate the long-term risk of their projects. As a medium-size car garage owner in Phnom Penh put it:

“I receive provincial regulations and laws from my friends. I have never contacted officials to get the information, because I don’t know where and who to ask for the information. I think most of the business owners don’t like to get the information affecting their business from government offices because it takes too much time... to help business get better access to information, the government should inform business owners publicly about the kind of information and who to contact. The effective measure is to disseminate the information directly via brochures to business owners, as this won’t cost much money because the government can use the tax collection from the business owners to pay for this.”

A working measure of transparency should therefore encompass the following four dimensions: access, equity, consistency, and predictability. The research team attempted to measure transparency according to these attributes by using the nine different indicators discussed below.



²² Kaufman, Daniel et al, 2002, 'Governance Matters', World Bank Policy Research Working Paper No. 2772, February, p. 5-7. Florini, Ann M.,1999, 'Does the Invisible Hand Need a Transparent Glove? The Politics of Transparency', paper prepared for the World Bank Conference on Development Economics, Washington, D.C., April;

5.3.1 Access to Information

The first attribute of transparency is access, which is defined as the timely dissemination of information. While legally, information on regulatory policy and provincial planning may be available to all, actually accessing that information is often problematic. In the Cambodian context, this can constrain private sector growth because firms may not be well positioned to take advantage of provincial initiatives.

Access also includes the availability of new laws, implementing documents, or provincial decisions. When changes in the legal regime are not readily accessible, a firm may operate illegally for several years. In most cases, such ignorance will not cost the firm very much, but there is always an increased chance that government officials extract unofficial fees. In PBES focus groups, firms noted this was often the case when it came to tax laws. Conversely, a firm may be eligible for savings, investment opportunities, or tax refunds, but never take advantage of them because it is unaware of the benefits. Even when information can be located, it is often opaque and unhelpful. The research team used two indicators to calculate access:

1. *Percentage of firms that did not know what the provincial budget was*
2. *Access to regulatory information*

• *Percentage of firms that did not know what the provincial budget was:* The research team took a unique approach to measuring access to information across the surveyed provinces. A list of the eleven provincial documents that are most vital to business operations was given to each firm. They were then asked to rate their access to these documents on a scale ranging from very easy to impossible.

In 2006, 35% or more of the firms did not

recognize six of the documents, which indicated severely limited transparency. Not only did firms lack access to documents that are supposedly publicly available, but many did not even know what they were. In 2009, knowledge of documentation has improved a great deal. This year there is not a single document with over 35% firms unaware of its existence and many documents (i.e. taxation policies and land titling) have very high recognition. Nevertheless, there is still room for improvement. Twenty-five percent of operations are unaware of two key types of business documentation, National Laws and the Provincial budget. The percentage of firms not recognizing the document presented to them is shown in the third column of Table 11.

To capture firms' limited knowledge of basic information, we used the percentage of firms from each province that did not know what the provincial budget was or why access to it would help their business. The highest figures were found in Kampong Chhnang (54.7%) and Pursat (50%). Awareness of the provincial budget was exceptionally high in Kampong Cham, where only 5.8% of firms were unaware of the provincial budget.

• *Access to regulatory information:* The research team then performed a factor analysis on these documents to see how closely they are related. Factor analysis is a procedure for reducing several highly correlated variables to a small number of uncorrelated variables. The loadings are the bivariate correlation between each of the different documents and the unobserved latent variable, which can be thought of as a general measure of access to all regulatory information. This simple fact allows us to calculate factor scores for each province, which represent overall access to regulatory documents. The result of the analysis was one factor (or basket) of documents that had very strong correlations with each other (shown by the Factor Loadings in the second column of Table 11).

Table 12 summarizes the results on the first dimension. According to firms, Kampong Cham has the highest access to documentation. Pursat, in which nearly 50% of firms did not

recognize what the provincial budget was, received the lowest score, indicating an urgent need for improvement.

Table 11: Important Provincial Documents and Firms’ Knowledge of Their Existence

| Type of Document | | Factor Loadings* | Firms that did not know document (%) |
|--|--|------------------|--------------------------------------|
| 1. | Information on which permits and stamps are required for business | 0.809 | 11% |
| 2. | Information on how to acquire operating licenses | 0.795 | 13% |
| 3. | Applications for business registration from Ministry of Commerce or Provincial Commerce Division | 0.774 | 17% |
| 4. | Information on Taxation | 0.529 | 7% |
| 5. | Provincial Budget (information on provincial expenditures & revenue collection) | 0.513 | 24% |
| 6. | National/Provincial investment incentive policies | 0.420 | 15% |
| 7. | Information on land titling | 0.392 | 8% |
| 8. | Land use allocation plans and maps (provincial zoning decisions for different types of lands) | 0.355 | 23% |
| 9. | National Government Laws and Prakas | 0.287 | 25% |
| 10. | Provincial Government policies | 0.179 | 20% |
| 11. | Plans for new infrastructure projects in province | 0.026 | 22% |
| <i>Eigen value / Percentage of Variance Explained</i> | | 4.46/41% | |
| *Factor Loadings are the result of a Factor Analysis procedure on 1234 firm responses with varimax rotation. Firms that answered they were unfamiliar with the document had their responses re-coded to 0. | | | |

Table 12 : Indicators Comprising Transparency (Dimension 1)
Access to Information

| Province | Access to Regulatory Information (Factor Analysis (Factor 1) | Don't Know whether Provincial Budget is Available (%) | Dimension Score* |
|---|--|---|------------------|
| Kampong Cham | 0.37 | 5.77% | 1.91 |
| Svay Rieng | 0.48 | 13.46% | 1.86 |
| Koh Kong | 0.25 | 7.50% | 1.79 |
| Takeo | 0.10 | 7.50% | 1.67 |
| Phnom Penh | 0.38 | 21.01% | 1.64 |
| Sihanoukville | 0.16 | 19.23% | 1.50 |
| Banteay Meanchey | -0.16 | 7.69% | 1.47 |
| Rattanakiri | -0.07 | 17.50% | 1.36 |
| Kandal | 0.11 | 28.85% | 1.29 |
| Siem Reap | -0.07 | 22.99% | 1.26 |
| Pailin | -0.04 | 25.00% | 1.25 |
| Stung Treng | -0.17 | 22.50% | 1.19 |
| Battambang | -0.36 | 16.47% | 1.15 |
| Kampong Chhnang | 0.47 | 54.72% | 1.09 |
| Kampong Thom | -0.35 | 20.00% | 1.09 |
| Prey Veng | -0.11 | 30.77% | 1.08 |
| Kampot | -0.32 | 23.08% | 1.07 |
| Mondulkiri | -0.34 | 25.00% | 1.02 |
| Kep | -0.29 | 27.50% | 1.01 |
| Preah Vihear | -0.33 | 27.50% | 0.97 |
| Kratie | -0.53 | 25.00% | 0.86 |
| Kampong Speu | -0.20 | 47.50% | 0.71 |
| Oddar Meanchey | -0.69 | 40.00% | 0.47 |
| Pursat | -0.68 | 50.00% | 0.29 |
| *Scores are re-scaled between .2 (1*.2) and 2 (10*.2), as this dimension represents 20% of the 10-Point sub-index. Factor scores were calculated using an approach similar to saving the predicted results of a regression, but taking the simple mean access per province yielded the exact same rank-ordering (i.e., statistically, they are perfectly correlated). For ease of interpretation, the mean scores are shown as well, but they were not used in the creation of the index. | | | |

5.3.2 Equity and Consistency of Application

While the two indicators above capture access to the documents, they do not necessarily represent equitable access, the lack of which can result in the inefficient use of provincial resources. Such inefficiencies can constitute more than a simple transfer of resources from one party to another. Take, for instance, the example of provincial planning. The beneficial impact of infrastructure and land conversion plans on the overall province is limited if their details are available to only a select few insiders. The firms that can access provincial documents may only be able to do so by exploiting favored connections to provincial government officials. Indeed, interviews with firms in many different provinces indicate the benefits of those with connections over those that did not have them. When business owners responded that access to business information was easy, further probing usually demonstrated that they meant it was easy for them because they knew someone in a provincial government office.

A medium-sized restaurant entrepreneur in Kampong Thom since 1986 shared her experience with obtaining information on rules and guidelines, and was quite open about her use of business contacts to obtain information, “I do think that it is easier to get the information if I have a friend or family member in the provincial government. Anyway, the easiest way to get the information is to contact them directly.” A guest-house owner in Rattanakiri reiterated the importance of direct visits to

provincial officials for business information, but drew a distinction between the need for direct contact when businesses need something from officials, and the many creative forms of publicity used when officials need something from businesses:

“When I need information related to business, such as information about tax and required licenses, I always visit relevant provincial departments. However, this information is always provided via the mouth of the officials in charge. I have never seen it on paper. In contrast, when the provincial departments need donations from business owners, they always distribute the donation information on paper to my place.”

The Rattanakiri owner felt that governments could benefit from publicly disseminating information, especially ones that are related to tax rates, via TV or radio, just as they do donation requests.

A follow-up question therefore sought to measure different aspects of equitable access in the transparency sub-index. Two variables used to capture equitable access are:

1. *The percentage of firms that considered a connection with someone in the provincial government to be important or very important in facilitating access to the above documents (Access to information dependent on a relationship with provincial government).*
2. *The percentage of firms that agreed or strongly agreed that favoritism toward firms with political connections is an obstacle to their business.*

Table 13 : Indicators Comprising Transparency (Dimension 2)
Equity and Consistency of Application

| Province | Access dependent on relationship with provincial government (%) | Favoritism toward firms w/ political connections is a business obstacle (%) | Dimension 2 Score* |
|--|---|---|--------------------|
| Pursat | 40.00% | 22.50% | 1.87 |
| Pailin | 45.00% | 17.50% | 1.86 |
| Preah Vihear | 47.50% | 20.00% | 1.76 |
| Kampot | 50.00% | 17.31% | 1.76 |
| Siem Reap | 47.13% | 24.14% | 1.70 |
| Prey Veng | 43.59% | 33.33% | 1.61 |
| Kep | 65.00% | 17.50% | 1.45 |
| Kampong Thom | 67.50% | 15.00% | 1.45 |
| Kratie | 47.50% | 40.00% | 1.42 |
| Battambang | 54.12% | 35.29% | 1.37 |
| Kampong Chhnang | 52.83% | 37.74% | 1.35 |
| Monduliri | 50.00% | 42.50% | 1.33 |
| Kampong Speu | 60.00% | 32.50% | 1.30 |
| Oddar Meanchey | 70.00% | 27.50% | 1.18 |
| Svay Rieng | 55.77% | 44.23% | 1.18 |
| Stung Treng | 45.00% | 57.50% | 1.17 |
| Banteay Meanchey | 55.77% | 51.92% | 1.05 |
| Koh Kong | 62.50% | 45.00% | 1.03 |
| Sihanoukville | 55.77% | 53.85% | 1.01 |
| Phnom Penh | 65.94% | 50.00% | 0.87 |
| Kandal | 51.92% | 67.31% | 0.86 |
| Rattanakiri | 62.50% | 55.00% | 0.86 |
| Takeo | 80.00% | 47.50% | 0.63 |
| Kampong Cham | 84.62% | 51.92% | 0.46 |
| *Scores are re-scaled between .2 (1*.2) and 2 (10*.2), as this dimension represents 20% of the 10-Point sub-index. | | | |

5.3.3 Predictability of Laws and Policies

The third dimension of transparency is predictability, or the notion that national laws and regulations are implemented in a consistent and foreseeable manner across the provinces. One important role of provincial government officials is to adequately inform firms about changes in national laws or in the implementation of those laws. Three indicators were used to capture whether firms understand how provincial decisions are made and how they will be implemented, so that they can gauge the direction of long-term strategies

and find it easier to make informed investment decisions. Table 14 demonstrates that most firms in Cambodia are poorly informed about national laws. Kampong Chhnang, Pailin, and Kampong Speu rank lowest in the sample when it comes to information provision, but no single province excels in this dimension. Table 14 summarizes the score for these indicators, which are as follows:

1. *Frequency of meetings between firms and representatives from the provincial governor’s office or province to discuss changes in laws or policies (% Seldom or Never)*

2. *Level of information on new rules, laws, and regulations that are related to economics and finance and/or that materially affect firms' business (% Not at all or Poorly)*
3. *Frequency of advance notification about changes in national government laws (% Seldom and Never)*

Table 14 : Indicators Comprising Transparency (Dimension 3)
Predictability of Laws and Policies

| Province | Firms that seldom or never meet with officials to discuss changes in law or policies (%) | Firms that have no or poor information on new rules, laws, and regulations (%) | Firms that seldom or never receive advance notice about changes in national government laws (%) | Dimension 3 Score* |
|------------------|--|--|---|--------------------|
| Sihanoukville | 65.38% | 53.85% | 40.38% | 1.93 |
| Koh Kong | 75.00% | 67.50% | 35.00% | 1.60 |
| Phnom Penh | 70.29% | 65.94% | 58.70% | 1.43 |
| Stung Treng | 70.00% | 60.00% | 67.50% | 1.42 |
| Takeo | 77.50% | 62.50% | 62.50% | 1.29 |
| Banteay Meanchey | 76.92% | 69.23% | 57.69% | 1.26 |
| Rattanakiri | 65.00% | 72.50% | 75.00% | 1.25 |
| Svay Rieng | 78.85% | 73.08% | 59.62% | 1.14 |
| Kampong Cham | 80.77% | 76.92% | 51.92% | 1.14 |
| Prey Veng | 74.36% | 61.54% | 84.62% | 1.10 |
| Pursat | 82.50% | 72.50% | 60.00% | 1.07 |
| Kep | 75.00% | 75.00% | 72.50% | 1.04 |
| Kratie | 82.50% | 62.50% | 75.00% | 1.04 |
| Kampot | 80.77% | 71.15% | 71.15% | 0.99 |
| Kampong Thom | 80.00% | 67.50% | 77.50% | 0.98 |
| Preah Vihear | 82.50% | 65.00% | 77.50% | 0.97 |
| Battambang | 81.18% | 74.12% | 74.12% | 0.90 |
| Monduliri | 85.00% | 65.00% | 80.00% | 0.89 |
| Kandal | 84.62% | 73.08% | 71.15% | 0.88 |
| Oddar Meanchey | 80.00% | 75.00% | 80.00% | 0.84 |
| Siem Reap | 82.76% | 81.61% | 78.16% | 0.71 |
| Kampong Chhnang | 94.34% | 77.36% | 67.92% | 0.66 |
| Kampong Speu | 92.50% | 80.00% | 82.50% | 0.49 |
| Pailin | 92.50% | 95.00% | 85.00% | 0.24 |

Scores are re-scaled between .2 (1.2) and 2 (10*.2), as this dimension represents 20% of the 10-Point sub-index.

5.3.4 Hard Data

The final dimension of transparency is derived from our own test for provincial information provision. Rather than relying solely on the perceptions of individual firms, the PBES research team traveled to all 24 of the sample provinces and, posing as private entrepreneurs, attempted to access applications for and

information about registration (from the Provincial Department of Commerce) and operating licenses (from the Provincial Department of Industry, Mines, & Energy).

We recorded the transparency of information from the departments on the following four-point scale (from 4 being good to 1 being bad):

4. Information is posted and applications are readily available without having to contact an official.
3. Information is clearly posted, but applications must be requested from an official.
2. Both information and application require requests to an official.
1. Requests that were made did not yield information or applications.

The third indicator in this section is simply a count of the number of provincial offices that have a map of planned infrastructure construction posted publicly. The more transparent the posting of such a map, the less likely it is possible that insiders can benefit by surreptitiously buying up cheap land around prospective infrastructure projects, before selling it at a profit after the building of the project. Current owners have a better sense of what their land is worth and current investors can construct long-term business plans with the

knowledge of the capacity of future infrastructure.

As Table 15 shows, through this exercise, Sihanoukville once again emerged as the most transparent province. All the necessary information was readily available in the foyer of the Department of Commerce, so there was no need for a firm to contact an official. Moreover, Sihanoukville had two separate offices with planned infrastructure maps available. This offers an interesting contrast to the survey results for Kampong Cham, which has relatively low access. Kampot and Oddar Meanchey had the least information available. In these three provinces, firms always had to contact provincial officials, and in at least one case, even after a request was made, the regulatory information never materialized.

Following our general rule, this hard data accounts for 40% of the transparency index.

Table 15 : Indicators Comprising Transparency (Dimension 4)
Independent Observation

| Province | Information request at Department of Commerce | Information request at Department of Industry, Mines, and Energy | Number of Office Where Infrastructure Maps are Publically Available | Dimension 4 Score* |
|------------------|---|--|---|--------------------|
| Sihanoukville | 4 | 2 | 2 | 3.1 |
| Rattanakiri | 3 | 3 | 1 | 2.8 |
| Siem Reap | 3 | 3 | 1 | 2.8 |
| Pailin | 5 | 1 | 2 | 2.8 |
| Koh Kong | 2 | 2 | 2 | 2.5 |
| Pursat | 2 | 2 | 2 | 2.5 |
| Stung Treng | 2 | 2 | 2 | 2.5 |
| Battambang | 3 | 2 | 1 | 2.2 |
| Banteay Meanchey | 2 | 3 | 0 | 1.9 |
| Kampong Cham | 1 | 1.5 | 2 | 1.9 |
| Monduliri | 2 | 2 | 1 | 1.9 |
| Takeo | 2 | 2 | 1 | 1.9 |
| Kampong Chhnang | 3 | 2 | 0 | 1.6 |
| Kep | 1 | 1 | 2 | 1.6 |
| Kampong Speu | 2 | 2 | 0 | 1.3 |
| Kampong Thom | 2 | 2 | 0 | 1.3 |
| Kandal | 2 | 2 | 0 | 1.3 |
| Kratie | 2 | 2 | 0 | 1.3 |
| Phnom Penh | 2 | 2 | 0 | 1.3 |
| Preah Vihear | 2 | 2 | 0 | 1.3 |
| Prey Veng | 2 | 2 | 0 | 1.3 |
| Svay Rieng | 2 | 2 | 0 | 1.3 |
| Kampot | 1 | 1 | 1 | 1 |
| Oddar Meanchey | 2 | 1 | 0 | 0.7 |

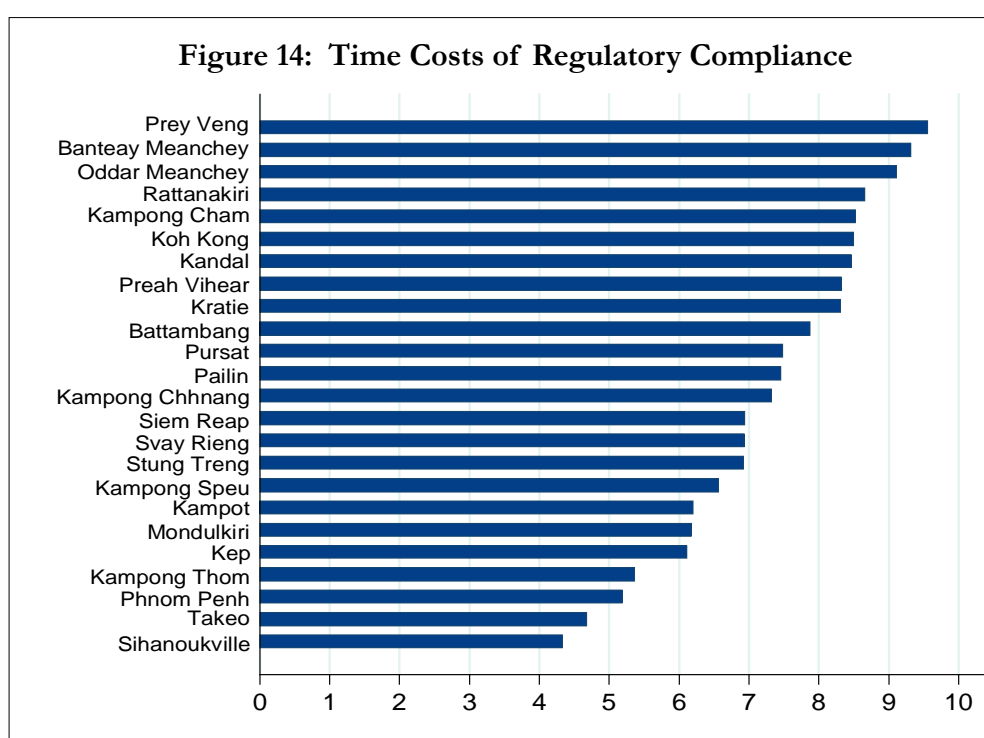
Scores are re-scaled between .4 (1.4) and 4 (10*.4), as this dimension represents 40% of the 10-Point sub-index.

5.4 Time Costs of Regulatory Compliance

The study of transaction costs in time has been an important element of economic transition literature. The old business maxim “time is money” is particularly relevant in the Cambodian provinces. Firm managers are often torn away from their business operations to deal with and attend to bureaucratic problems. When this occurs, they lose valuable time that could be more productively spent managing their company operations. In addition, the 2009 ICA points out that excessive regulation can

- *Bureaucratic procedures:* To create this indicator we asked the question, “In a typical week in the last year, what percentage of the total time of owners or high-level managers was spent on dealing with requirements imposed by government regulations [e.g., taxes, customs, labor regulations, licensing and registration, including dealings with officials, completing forms, etc.]?”

This question is generally asked by the ICA researchers in the form of a five-point Likert scale. Unfortunately, firms in the PBES focus



lead to higher risk avoidance and a preference for remaining in the informal economy and avoiding such burdens.

The survey considered three indicators of time costs, which are weighted equally:

1. *Management time spent on bureaucratic procedures (median days)*
2. *Median number of regulatory inspections in past year*
3. *Wait for formal land title (median days)*

groups had trouble calculating percentages. As a result, they were asked to record the total number of days during the year that they had spent on such procedures, and annual averages were calculated using those responses. The percentage of firms that spent over 16 days (4.5% of a year) of senior management’s annual activity on bureaucratic procedures was taken as the final indicator.

Overall, there has been a notable increase in the amount of time firms spend on bureaucratic

procedures throughout the country. In the median province, the number of firms spending over 16 days on such activities has risen from 15% to 27%. For the second straight year, however, Banteay Meanchey proved that its businesses face very little regulatory burdens, with 0% of operations spending over 16 days on regulatory procedures. By contrast, 41% of firms in Phnom Penh and 43% in Kampong Speu spent over 16 days on such procedures.

In half of the Cambodian provinces, total inspections do not appear to be a tremendous burden with firms facing on average only two inspections to their businesses per year. This is a tremendous improvement from 2006 where the median number of inspections per year was four. Inspections appear to be excessive, however, in Mondulkiri (12) and Takeo (12). Our survey shows that the length of these inspections was short – often less than an hour – and did not vary regionally.

Table 16 : Average Inspections by Provincial Agency

| Agency | Mean | Lower Bound | Upper Bound |
|---------------------------|-------|-------------|-------------|
| Tax Inspectorate | 1.78 | 1.40 | 2.17 |
| Labor and Social Security | 0.24 | -0.09 | 0.57 |
| Fire and Building Safety | 1.03 | 0.71 | 1.36 |
| Sanitation/Epidemiology | 0.71 | 0.50 | 0.92 |
| Police | 11.69 | 4.10 | 19.29 |
| Environment | 0.29 | 0.14 | 0.44 |
| Customs | 0.05 | 0.02 | 0.09 |

- Inspections policy:* A common complaint made by private firms is that inspections policy remains a burden. Provincial agencies inspect firms too frequently and their inspections are excessively long. Of course inspections are necessary to some extent, especially as Cambodia attempts to move to a full regulatory system. As more environmental, health, and, safety licenses that apply to initial business activities are being removed, the responsibility for ensuring that such private firms continuously meet such standards is shifting to regulatory agencies. A key challenge for these bodies is how to manage their responsibilities effectively while also inexpensively. Interestingly, Table 16 shows tax officers and the police, rather than regulatory agencies, conducted the majority of inspections.

- Wait for formal land title:* The final indicator measures the median number of days it took firms to receive their formal land titles from the time they received their land and submitted their applications. It provides an excellent picture of the bureaucratic efficiency of provincial authorities.

Data from these three indicators and the final Time Costs of Regulatory Compliance Index are shown in Table 17. Prey Veng was found to have the least bureaucratic barriers, while Phnom Penh, Takeo, Sihanoukville impose the lengthiest procedures. Sihanoukville has reasonable scores on two of the indicators but seems particularly bad at allocating land titles in a timely manner.

Table 17: Indicators Comprising Time Costs of Regulatory Compliance

| Province | Firms spending over 16 days per year on bureaucratic procedures (%) | Total Inspections Annually (Median) | Wait for land title (Median Days) | Time Costs Sub-index Score* |
|------------------|---|-------------------------------------|-----------------------------------|-----------------------------|
| Prey Veng | 0.00% | 0 | 30 | 9.56 |
| Banteay Meanchey | 0.00% | 1 | 30 | 9.31 |
| Oddar Meanchey | 8.33% | 1 | 10 | 9.11 |
| Rattanakiri | 6.25% | 3 | 15 | 8.66 |
| Kampong Cham | 11.76% | 2 | 15 | 8.53 |
| Koh Kong | 8.11% | 2 | 30 | 8.50 |
| Kandal | 14.00% | 0.5 | 30 | 8.47 |
| Preah Vihear | 14.29% | 1 | 30 | 8.32 |
| Kratie | 0.00% | 5 | 30 | 8.31 |
| Battambang | 17.07% | 2 | 30 | 7.88 |
| Pursat | 30.56% | 1 | 15 | 7.48 |
| Pailin | 0.00% | 6.5 | 55 | 7.46 |
| Kampong Chhnang | 26.92% | 1.5 | 30 | 7.32 |
| Siem Reap | 26.39% | 2 | 45 | 6.95 |
| Svay Rieng | 30.61% | 2 | 30 | 6.94 |
| Stung Treng | 24.24% | 5 | 15 | 6.92 |
| Kampong Speu | 43.24% | 0 | 30 | 6.56 |
| Kampot | 34.00% | 4 | 30 | 6.20 |
| Mondulkiri | 11.76% | 12 | 7 | 6.18 |
| Kep | 20.00% | 6 | 60 | 6.11 |
| Kampong Thom | 36.11% | 4.5 | 60 | 5.36 |
| Phnom Penh | 40.52% | 4 | 60 | 5.18 |
| Takeo | 21.62% | 12 | 50 | 4.68 |
| Sihanoukville | 31.25% | 2 | 165 | 4.33 |

*Scores are re-scaled between 1 and 10

5.5 Informal Charges

The four quotes from entrepreneurs in the accompanying text box illustrate the range of experiences and opinions about informal charges in the Cambodian business environment. For some entrepreneurs, it is a tremendous burden that they feel obligated to pay. Others believe that bribes are not necessary but do expedite business transactions. Finally, some believe that the need for informal charges has declined over time as a result of procedural simplification that reduces the amount of contacts with provincial officials.

Our research in 2006 revealed that informal charges in Cambodia should be considered in three dimensions. The first is micro-corruption, which occurs when businesses pay small bribes to obtain favorable official decisions, expedite bureaucratic procedures and pass regulatory inspections. Micro-corruption is a major problem for domestic investors, as unwarranted delays can cut into firms’ profits. One focus group participant claimed that a number of officials considered informal payments to facilitate government procedures as “normal.” During inspections, officials charge firms small “fees,” expect gifts (beer or cigarettes)

in exchange for positive inspection results, or assign fines and penalties that are difficult for firms to appeal in a non-transparent manner. Firms in the PBES focus groups claimed to understand that one of the reasons for micro-corruption is the low salaries that provincial agencies pay their officials, who then expect “tips,” but they also complained about some officials who often ask for payments far beyond the means of small entrepreneurs. It is worth noting that some firms acknowledged paying bribes to build connections for illicit purposes as well as for normal business activities. Such payments often enable businesses to receive advance warnings of impending police raids, engage in illegal or unauthorized behavior, and avoid paying higher taxes.

Macro-corruption, the second dimension, relates to bribe requests made by higher ranking officials who are involved in the bidding for public procurement contracts. Such bribes are often assessed as a percentage of the contract or quota amounts, and can reach a sum of hundreds of thousands of dollars. Moreover, the bidding process tends to be unfair and stacked against firms that lack connections.

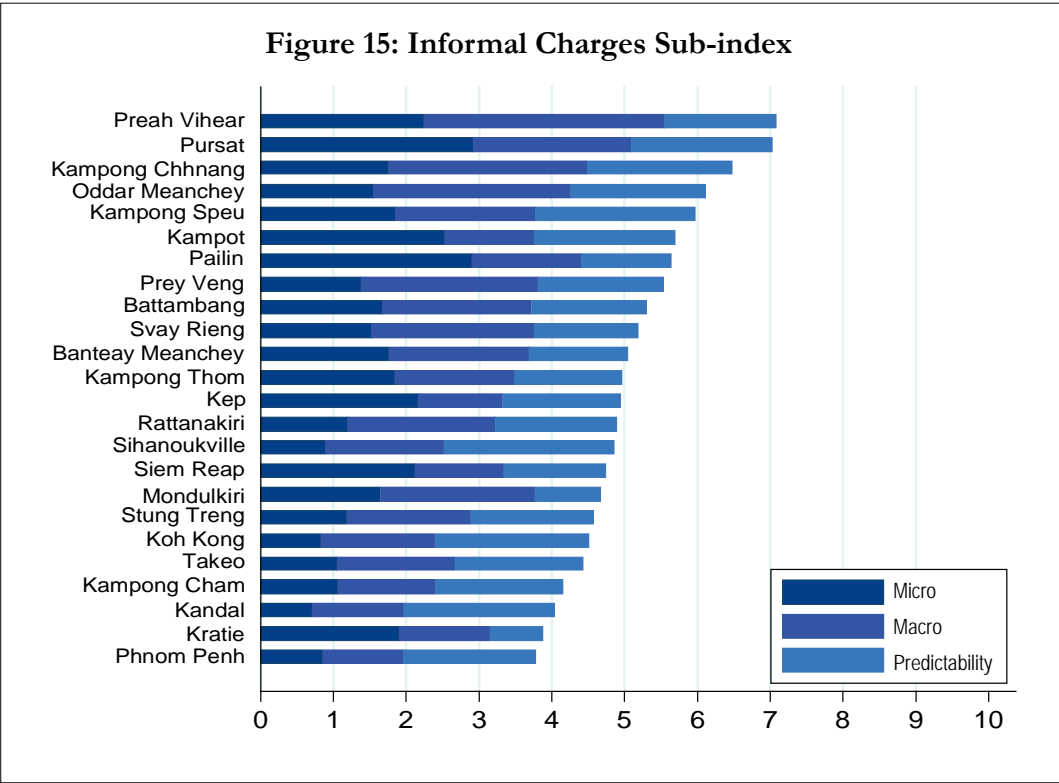
A third dimension of informal charges measures the predictability of corrupt actions. A wide range of literature on corruption indicates that firms may consider informal charges beneficial if these expedite bureaucratic procedures and are predictable (i.e., enable firms to factor bribe costs into their business plans and deliver the expected results). In Cambodia, Malesky and Samphantharak (2008) have shown that predictability of the bribe schedule is more important for business investment than the size of bribes paid by entrepreneurs.

While most firms in our focus groups claimed that they could not predict extra payments exactly, there was some consensus that threshold prices exist for most types of assistance from

provincial officials. Any payment less than \$5 for a small firm or \$20 for a larger firm would be too low to yield the desired outcome. Such charges are based on the notion that firms network and, over time, learn from both their own and their peers’ experiences about what they are paying for, how much it should cost, and (most importantly) whether they will eventually receive the service that they need.

Spectrum of Experiences with Informal Charges in Cambodian Provinces

1. *Small-scale car garage entrepreneur in Ratanakiri province: “I’ve checked with other garages similar to mine and I found out that I always pay 50% higher taxes (patent and monthly taxes) compared to them. Although I am upset about this, I still agree to pay that rate because I don’t want to have any problem with local authorities.”*
2. *Medium-sized car garage in Phnom Penh: “We cannot avoid informal charges when dealing with government officials. We have to spend more or less depending on the case and person. I’ve paid informal charges even to obtain licenses, tax payment, fire inspection and inspection by economic police. I think the officials’ low salary and the heavy bureaucratic and ineffective procedures are the main cause of corruption. Thus, without informal fee, we can’t get things done as we want to.”*
3. *Medium-scale foreign language center entrepreneur in Kratie province. “Officials do not set the fee for the informal charge in this province. We are free to give or not to give them the informal fee. For me, to speed up the process of getting my license, I paid some informal fee.”*
4. *Medium-sized brick and tile factory in Kampong Cham province. “Actually, the informal charge has been sharply reduced. I think the simple bureaucratic procedures help reduce the corruption.”*



5.5.1 Micro-Corruption

Three indicators measure the extent of the problem by gauging the frequency, type, and amount of extra payments:

1. *The percentage of firms that believe that enterprises in their line of business are subject to bribes from provincial authorities.* Note that this question was phrased so that firms were answering about firms in general as opposed to their own experience with bribes – thereby substantially increasing the response rate.
2. *The percentage of firms that consider corruption to be a major or severe obstacle* is used as a simple measure of the burden that extra payments impose on firms in the sample.
3. *The percentage of firms that agree that paying bribes is useful for business* traces the utility of informal charges for private entrepreneurs.

Table 18 demonstrates that micro-corruption poses the least difficulty in Pursat and the greatest in Kandal.

Table 18: Indicators Comprising Informal Charges (Dimension 1)
Micro-Corruption

| Province | Enterprises in my line of business do not make extra payments (%) | Corruption is a major or severe obstacle (%) | Bribes are Useful for Businesses (%) | Dimension 1 Score* |
|---|---|--|--------------------------------------|--------------------|
| Pursat | 75.00% | 10.00% | 10.00% | 2.92 |
| Pailin | 97.50% | 20.00% | 17.50% | 2.90 |
| Kampot | 73.08% | 19.23% | 15.38% | 2.53 |
| Preah Vihear | 72.50% | 22.50% | 22.50% | 2.25 |
| Kep | 75.00% | 25.00% | 25.00% | 2.17 |
| Siem Reap | 60.92% | 14.94% | 25.29% | 2.12 |
| Kratie | 77.50% | 22.50% | 37.50% | 1.91 |
| Kampong Speu | 55.00% | 22.50% | 25.00% | 1.86 |
| Kampong Thom | 72.50% | 47.50% | 17.50% | 1.85 |
| Banteay Meanchey | 82.69% | 42.31% | 30.77% | 1.76 |
| Kampong Chhnang | 56.60% | 16.98% | 33.96% | 1.75 |
| Battambang | 68.24% | 32.94% | 31.76% | 1.68 |
| Mondulkiri | 67.50% | 32.50% | 32.50% | 1.65 |
| Oddar Meanchey | 70.00% | 42.50% | 30.00% | 1.55 |
| Svay Rieng | 63.46% | 42.31% | 26.92% | 1.53 |
| Prey Veng | 64.10% | 41.03% | 33.33% | 1.38 |
| Rattanakiri | 55.00% | 30.00% | 42.50% | 1.20 |
| Stung Treng | 50.00% | 52.50% | 22.50% | 1.18 |
| Kampong Cham | 48.08% | 55.77% | 23.08% | 1.06 |
| Takeo | 75.00% | 50.00% | 45.00% | 1.05 |
| Sihanoukville | 53.85% | 55.77% | 32.69% | 0.89 |
| Phnom Penh | 44.93% | 41.30% | 39.13% | 0.86 |
| Koh Kong | 42.50% | 52.50% | 30.00% | 0.83 |
| Kandal | 50.00% | 48.08% | 42.31% | 0.71 |
| *Scores are re-scaled between .33 (1*.333) and 3.33 (10*.333), as this dimension represents 1/3% of the 10-Point sub-index. | | | | |

5.5.2 Macro-Corruption

The three indicators that make up our measure of macro-corruption as it relates to public procurement contracts were chosen to cover the entire bidding process.

1. *Level of belief that information regarding available public procurement contracts is transparent (% Often or Always).*
2. *Level of importance of personal connections to government officials for winning public procurement contracts (% Important or Very Important).*
3. *Frequency of payment of commissions of firms in the same line of business to do business with the government (% Never or Seldom)*

Do all firms have equal information about the opportunity for such contracts? If a firm puts in a bid does it have a fair chance of obtaining the contract? Are bribes expected to facilitate a winning bid? Given the unsophisticated nature of the firms in the sample, there was concern during the survey design stage that firms would not know enough about public procurement to answer these questions. As a result, a “Don’t know” option was provided. Thirty-five point six percent of firms used the “Don’t know” response on questions of extra payments in bidding for public contracts, but none chose it on the preceding two questions. The simple reason for this apparent contradiction is that procurement is much more widespread than

Table 19: Indicators Comprising Informal Charges (Dimension 2)
Macro-Corruption

| Province | Public procurement contracts are often or always transparent (%) | Connections are important for winning public procurement contracts (%) | Firms never or seldom pay commissions when doing business with government (%) | Dimension 2 Score* |
|------------------|--|--|---|--------------------|
| Preah Vihear | 30.00% | 40.00% | 66.67% | 3.30 |
| Kampong Chhnang | 24.53% | 39.62% | 40.00% | 2.74 |
| Oddar Meanchey | 20.00% | 45.00% | 57.89% | 2.70 |
| Prey Veng | 20.51% | 56.41% | 60.00% | 2.43 |
| Svay Rieng | 19.23% | 59.62% | 55.81% | 2.23 |
| Pursat | 20.00% | 50.00% | 32.00% | 2.17 |
| Mondulkiri | 25.00% | 60.00% | 36.00% | 2.11 |
| Battambang | 30.59% | 64.71% | 28.13% | 2.05 |
| Rattanakiri | 22.50% | 67.50% | 50.00% | 2.03 |
| Banteay Meanchey | 26.92% | 65.38% | 29.41% | 1.93 |
| Kampong Speu | 15.00% | 50.00% | 26.09% | 1.92 |
| Stung Treng | 12.50% | 72.50% | 59.26% | 1.70 |
| Kampong Thom | 17.50% | 65.00% | 30.77% | 1.65 |
| Sihanoukville | 18.37% | 60.00% | 18.18% | 1.63 |
| Takeo | 10.00% | 70.00% | 54.55% | 1.62 |
| Koh Kong | 22.50% | 57.50% | 0.00% | 1.56 |
| Pailin | 5.00% | 57.50% | 34.78% | 1.51 |
| Kampong Cham | 26.92% | 75.00% | 8.89% | 1.35 |
| Kandal | 5.77% | 61.54% | 23.68% | 1.26 |
| Kratie | 0.00% | 62.50% | 36.84% | 1.24 |
| Kampot | 1.92% | 59.62% | 26.32% | 1.23 |
| Siem Reap | 5.75% | 63.10% | 23.81% | 1.21 |
| Kep | 2.50% | 65.00% | 30.77% | 1.16 |
| Phnom Penh | 14.81% | 72.26% | 13.40% | 1.10 |

Scores are re-scaled between .33 (1.333) and 3.33 (10*.333), as this dimension represents 1/3% of the 10-Point sub-index.

it would seem, with many provincial agencies ordering construction, repair services, sign-making, and food delivery from local vendors. We concluded from this that firms were familiar with the concept of public procurement but chose “Don’t know” to avoid answering the sensitive question of whether they had paid bribes to win contracts. Due to this phenomenon, when the research team calculated the percentage of firms that never or seldom pay bribes, the firms that answered “Don’t know” were considered part of the relevant sample rather than as missing data.

Preah Vihear and Kampong Chhnnang demonstrate the lowest evidence of macro-

corruption in Table 19. By contrast, Phnom Penh and Kep appears to have the greatest difficulty with macro-corruption.

5.5.3 Predictability of Informal Charges

To obtain a more accurate measure of corruption in the Cambodian context and to test the implications that corruption has for investment, we created a final measure for the predictability of informal charges. It is made up of three indicators:

1. *The percentage of firms answering that they know the amount of extra payments in advance.*

2. *The percentage of firms agreeing that after payments, the relevant service was delivered as expected.*
3. *The percentage of firms that say that once other government agencies have heard that a firm has paid an additional fee, are they not more likely to ask for ‘additional payments’ themselves.*

As with unpredictable fees, private firms cannot calculate whether making a payment to one agency will cause them to have to make future payments to other agencies, and therefore their ability to forecast their expected corruption costs is limited. For this reason, the research team considered the percentage of firms that answered no to this question as analogous to the predictability of fees charged by individual inspectors.

Table 20 illustrates that corruption is least predictable in Mondulkiri and Kratie and highly predictable in Sihanoukville and Kampong

Speu. More research may certainly help sort out this puzzle.

5.6 Participation

Participation represents the flip-side of Transparency. While Transparency indicates how much information provinces voluntarily supply to entrepreneurs, Participation studies provincial officials’ receptiveness to the information provided by firms about changes in provincial policies and initiatives. The accompanying text box derived from our interviews with businesses gives some sense of the scope and issues involved in participation.

This Sub-index measures if firms are consulted during the creation of provincial policies, either through individual discussions with government officials, forums between the government and enterprises, and/or through advocacy on the

Table 20: Indicators Comprising Informal Charges (Dimension 3)
Predictability of Corruption

| Province | After payment, service was delivered as expected | Firms who know the amount of extra payment in advance (%) | After payment, other agencies are less likely to ask for their own extra payments (%) | Dimension 3 Score* |
|------------------|--|---|---|--------------------|
| Sihanoukville | 42.31% | 38.46% | 57.69% | 2.34 |
| Kampong Speu | 15.00% | 7.50% | 42.50% | 2.19 |
| Koh Kong | 45.00% | 42.50% | 47.50% | 2.12 |
| Kandal | 30.77% | 30.77% | 48.08% | 2.07 |
| Kampong Chhnang | 22.64% | 7.55% | 20.75% | 1.99 |
| Kampot | 32.69% | 25.00% | 28.85% | 1.93 |
| Pursat | 22.50% | 12.50% | 25.00% | 1.93 |
| Oddar Meanchey | 10.00% | 5.00% | 27.50% | 1.85 |
| Phnom Penh | 33.33% | 35.51% | 37.68% | 1.83 |
| Takeo | 17.50% | 12.50% | 22.50% | 1.75 |
| Kampong Cham | 46.15% | 42.31% | 25.00% | 1.75 |
| Prey Veng | 15.38% | 5.13% | 12.82% | 1.72 |
| Stung Treng | 27.50% | 30.00% | 30.00% | 1.68 |
| Rattanakiri | 25.00% | 30.00% | 32.50% | 1.66 |
| Kep | 10.00% | 15.00% | 30.00% | 1.63 |
| Battambang | 21.18% | 27.06% | 29.41% | 1.59 |
| Preah Vihear | 10.00% | 10.00% | 17.50% | 1.54 |
| Kampong Thom | 10.00% | 17.50% | 25.00% | 1.47 |
| Svay Rieng | 26.92% | 42.31% | 34.62% | 1.42 |
| Siem Reap | 20.69% | 32.18% | 27.59% | 1.40 |
| Banteay Meanchey | 19.23% | 23.08% | 13.46% | 1.35 |
| Pailin | 7.50% | 12.50% | 7.50% | 1.22 |
| Mondulkiri | 10.00% | 25.00% | 5.00% | 0.91 |
| Kratie | 12.50% | 32.50% | 2.50% | 0.73 |

Scores are re-scaled between .33 (1.333) and 3.33 (10*.333), as this dimension represents 1/3% of the 10-Point sub-index.

part of business associations. Because a great deal of effort has recently been made toward empowering associations to advocate on behalf of the private sector, we have focused specifically on this element of governance.

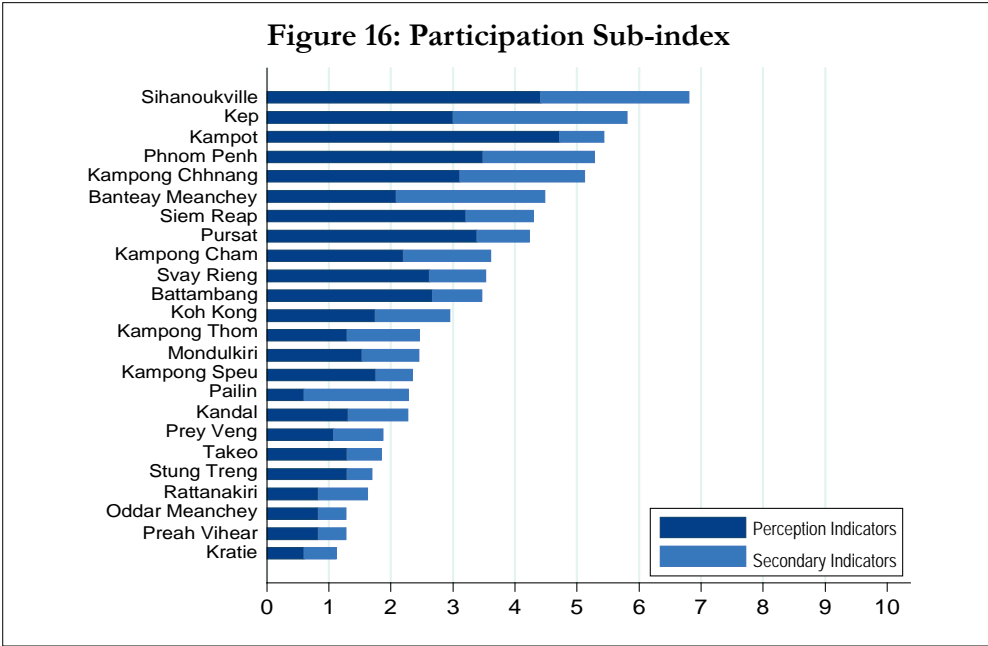
Three indicators comprise the Perceptions dimension of the Participation Sub-index:

- 1. *When a new law, rule, regulation or decree that could have a substantial impact on your business is being discussed, does the provincial government solicit advice from firms like yours regarding the legal document's content or implementation? (% Always or Regularly).*
- 2. *Percentage of firms that could identify active business associations in their province, whether or not they belonged to any. This indicator is a measure of business associations' visibility.*
- 3. *Percentage of firms from the PBES sample who are members of business associations. This statistic measures the organizations' inclusiveness.*

The answer to the first question directly indicates firms' evaluations of their roles in provincial decision making. Compared to levels of participation in neighboring Vietnam, scores

Participation in Cambodian Provinces

- 1. *Medium-scale foreign language center in Kratie province: "I have never been consulted when they want to create a new business policy. I think I've been excluded because they may think my business is small and not important. Actually, I do want to provide my input on business policies as it's a good time for me to express my concern."*
- 2. *Medium-sized restaurant owner in Svay Rieng province. "I have never been consulted when they want to issue new business regulations and policies. I think if we had a business association, it would be better. Because we will have a bigger voice and the provincial government would integrate our comments into the new business policies. I think the provincial government should consult with business owners before preparing new business regulations and policies."*
- 3. *Medium-sized brick and tile factory owner in Kampong Cham province: "I used to provide input and comments on business policies to my provincial officials via our brick and tile association in provincial private sector forum. The association is very important for brick and tile owners as it helps gather all the owners to meet and share information. More importantly, it has bigger voice to deal with the government."*



in each Cambodian province were low. The highest value, in Sihanoukville, was only 9.6%. Indicators two and three capture the role of business associations in provincial activities. Although business associations fulfill a variety of roles, one of their primary purposes is to advocate on behalf of the private sector.

Table 21 displays relatively high firm perceptions of participation for Kampot and Sihanoukville. By contrast, Kratie and Pailin had the worst scores possible with zero participation in decision making and no members active in business associations.

Three further indicators comprise the hard data dimension of the Participation Sub-index :

- Business associations for every 1,000 firms.*
This hard data measure of associations’

outreach captures the number of business associations registered with the DOC and DIME in every province.

- Business Forums held in 2007* captures the amount of public opportunities entrepreneurs had to interact with provincial officials to discuss changes in policy or offer suggestions. Most provinces didn’t hold any such forums, but Banteay Meanchey and Sihanoukville were very active with 21 total events.
- Communication Mechanisms.* Finally, we count the number of communications mechanisms for firms to interact with commune council members and other agencies. These mechanisms include suggestion boxes outside provincial agencies as well as telephone numbers to call in case of business problems.

Table 21: Indicators Comprising Participation (Dimension 1)
Perceptions Data

| Province | Firms regularly or always participating in decision making (%) | Firms able to identify business associations in province (%) | Self-identified members of business associations in province (%) Ψ | Dimension 1 Score* |
|------------------|--|--|---|--------------------|
| Kampot | 7.69% | 9.62% | 6% | 4.72 |
| Sihanoukville | 9.62% | 15.38% | 2% | 4.42 |
| Phnom Penh | 2.17% | 19.57% | 2% | 3.49 |
| Pursat | 7.50% | 15.00% | 0% | 3.38 |
| Siem Reap | 2.30% | 8.05% | 5% | 3.21 |
| Kampong Chhnang | 3.77% | 13.21% | 2% | 3.11 |
| Kep | 5.00% | 7.50% | 3% | 3.01 |
| Battambang | 5.88% | 10.59% | 0% | 2.68 |
| Svay Rieng | 1.92% | 11.54% | 2% | 2.62 |
| Kampong Cham | 3.85% | 9.62% | 0% | 2.20 |
| Banteay Meanchey | 0.00% | 9.62% | 2% | 2.08 |
| Kampong Speu | 2.50% | 7.50% | 0% | 1.76 |
| Koh Kong | 0.00% | 12.50% | 0% | 1.75 |
| Monduliri | 5.00% | 0.00% | 0% | 1.54 |
| Kandal | 1.92% | 3.85% | 0% | 1.31 |
| Kampong Thom | 2.50% | 2.50% | 0% | 1.30 |
| Stung Treng | 2.50% | 2.50% | 0% | 1.30 |
| Takeo | 2.50% | 2.50% | 0% | 1.30 |
| Prey Veng | 2.56% | 0.00% | 0% | 1.08 |
| Preah Vihear | 0.00% | 2.50% | 0% | 0.83 |
| Rattanakiri | 0.00% | 2.50% | 0% | 0.83 |
| Oddar Meanchey | 0.00% | 2.50% | 0% | 0.83 |
| Kratie | 0.00% | 0.00% | 0% | 0.60 |
| Pailin | 0.00% | 0.00% | 0% | 0.60 |

Scores are re-scaled between .6 (1.6) and 6 (10*.6), as this dimension represents 60% of the 10-Point sub-index

Ψ : Firms answering Don't Know were re-coded to No.

Table 22: Indicators Participation (Dimension 2)
Hard Data

| Province | Business Associations per 10,000 Firms | Business Forums Held in 2007 | Participation Mechanism (Suggestion Boxes or Communication Mechanism to Communal Councils) | Dimension 2* |
|--|--|------------------------------|--|--------------|
| Kep | 55.56 | 0.00 | 3.00 | 2.80 |
| Banteay Meanchey | 0.00 | 21.00 | 2.00 | 2.40 |
| Sihanoukville | 0.00 | 21.00 | 2.00 | 2.40 |
| Kampong Chhnang | 6.17 | 5.00 | 3.00 | 2.02 |
| Phnom Penh | 1.41 | 3.00 | 3.00 | 1.80 |
| Pailin | 24.88 | 6.00 | 1.00 | 1.68 |
| Kampong Cham | 17.97 | 4.00 | 1.00 | 1.42 |
| Koh Kong | 0.00 | 7.00 | 1.00 | 1.20 |
| Kampong Thom | 16.75 | 0.00 | 1.00 | 1.16 |
| Siem Reap | 26.62 | 2.00 | 0.00 | 1.09 |
| Kandal | 2.24 | 2.00 | 1.00 | 0.96 |
| Mondulkiri | 0.00 | 2.00 | 1.00 | 0.91 |
| Svay Rieng | 4.93 | 0.00 | 1.00 | 0.91 |
| Pursat | 0.00 | 1.00 | 1.00 | 0.86 |
| Rattanakiri | 0.00 | 0.00 | 1.00 | 0.80 |
| Battambang | 13.00 | 2.00 | 0.00 | 0.80 |
| Prey Veng | 12.98 | 2.00 | 0.00 | 0.79 |
| Kampot | 9.43 | 2.00 | 0.00 | 0.72 |
| Kampong Speu | 6.33 | 1.00 | 0.00 | 0.59 |
| Takeo | 6.74 | 0.00 | 0.00 | 0.55 |
| Kratie | 0.00 | 2.00 | 0.00 | 0.51 |
| Preah Vihear | 0.00 | 1.00 | 0.00 | 0.46 |
| Oddar Meanchey | 0.00 | 1.00 | 0.00 | 0.46 |
| Stung Treng | 0.00 | 0.00 | 0.00 | 0.40 |
| *Scores are re-scaled between .4 (1*.4) and 4 (10*.4), as this dimension represents 40% of the 10-Point sub-index. | | | | |

5.7 Crime Prevention

Any quick glance at a Cambodian daily newspaper will reveal that crime (sometimes violent) is a common occurrence. The constant threat of crime also affects the decisions of entrepreneurs. Indeed, our focus group demonstrated that crime was an issue in almost all provinces, though its relative importance varied. A tractor and motor retailer in one province was particularly graphic in his depiction of crime and its effect on business:

“The security situation in this province is not good because there have been armed robberies. Last year, a

jewelry shop was robbed and the owner was shot. The owner called the provincial police and they came but the robbers had left. The robbers haven’t been caught yet. Now, businesses in this province try to protect themselves by reducing the operating hours. Because of the security situation in the province, people are scared to go out at night or even in the evening. This affects businesses and economy of the province badly.

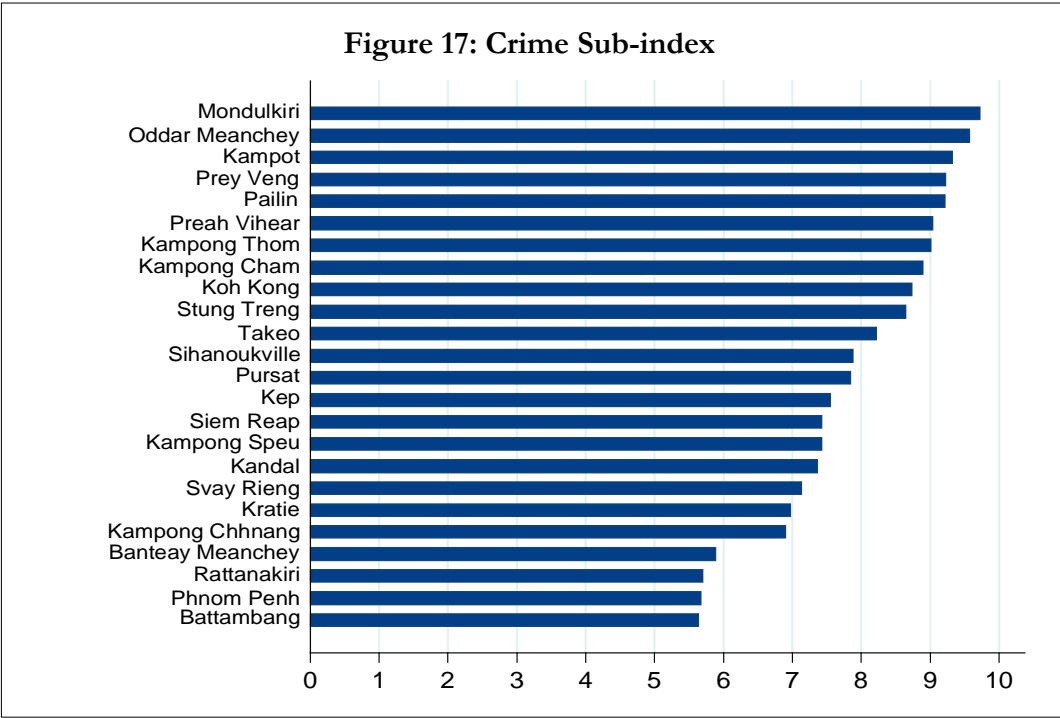
For me, to protect my business from robbers, I’ve made a good relationship with the police chief here. I always send him presents on special occasions and, sometimes, treat or give some money to their subordinates. I think the provincial police should strengthen the patrol every night.”

While firms in Mondulkiri, Oddar Meanchey, appear satisfied with the level of protection that provincial governments offered, firms in Cambodia’s two most populous areas Phnom Penh and Sihanoukville were much more anxious about the increasing numbers of violent crime and robbery. In Siem Reap and Sihanoukville, entrepreneurs worried less about robberies than about the growing criminal drug trade and its potentially negative impact on tourism. Crime is expensive for firms, even if they never actually experience a robbery. Many firms pay individuals to act as security guards on their premises, while others not, firms even pay police officers to protect their business. As a business owner in Kampong Cham exclaimed, “...business owners have tried to protect their properties by themselves by attaching more doors to the existing one and using more locks.”

With this in mind, we developed four indicators of crime prevention for each province:

1. *The percentage of firms that did not experience a robbery, vandalism, or arson in the last year.*
2. *The value of losses from firms that did experience a crime.*

3. *The percentage of firms paying protection money directly to police officers.*
 4. *Percentage of firms paying protection money to other individuals and organizations.*
- *The percentage of firms that did not experience a robbery, vandalism, or arson in the last year* is used to measure the scope of crime in a province. The majority of firms were untouched by crime last year, with the notable exception being businesses in Kandal, which had the highest number of crimes for the second year in a row. Forty percent of firms within its borders were affected by some type of criminal activity in 2007.
 - *The value of losses from firms that did experience a crime.* Median losses from affected businesses ranged from \$30 in Kampot, which had the lowest material costs for the second year in a row, to \$1025 in Kep province.
 - *Percentage of firms paying protection money directly to police officers.* Police officers are generally the most common recipients of protection-related payments, even though our focus groups indicated that their impact on crime



prevention was limited. Over 30% of firms in Phnom Penh admit this activity.

- *Percentage of firms paying protection money to other individuals and organizations.*

Table 23 demonstrates that crime poses the least difficulty for firms in the eastern provinces of Mondulkiri and Oddar Meanchey. It is, however, a severe burden for businesses in Phnom Penh and Battambang.

5.8 Tax Administration and Burden

Interviews with firms indicate that the Cambodian tax administration system, because it can be so cumbersome and expensive, has

incentivized participation of both businesses and tax collectors in a complex web of informal activity that primarily benefits individual tax inspectors and selected firms. It deprives provincial governments of revenue, makes firms dependent on provincial authorities (because the firms’ growth corresponds with a proportionate increase in payments), and denies individual citizens public services that could be provided through a larger tax base.

For example, a barbershop in Kampong Speu explained that paying taxes was not expensive or time-consuming, taking only about 15 minutes, it is just unnecessary. After getting to know tax officials better, he simply stopped paying the assessments.

Table 23: Indicators Comprising Crime Prevention Sub-index

| Province | Firms that did not experience a robbery (%)Ω | Losses of firms that did experience robbery (Median \$) | Firms paying protection money to provincial police (%) | Firms paying protection money to other groups or organizations (%) | Sub-index Score* |
|--|--|---|--|--|------------------|
| Mondulkiri | 94.12% | 65.00 | 0.00% | 0.00% | 9.73 |
| Oddar Meanchey | 97.22% | 50.00 | 5.00% | 0.00% | 9.59 |
| Kampot | 86.00% | 30.00 | 0.00% | 0.00% | 9.32 |
| Prey Veng | 97.06% | 200.00 | 5.13% | 0.00% | 9.23 |
| Pailin | 86.84% | 100.00 | 0.00% | 0.00% | 9.21 |
| Preah Vihear | 91.43% | 300.00 | 0.00% | 0.00% | 9.04 |
| Kampong Thom | 88.89% | 245.00 | 0.00% | 0.00% | 9.01 |
| Kampong Cham | 86.27% | 100.00 | 3.85% | 0.00% | 8.90 |
| Koh Kong | 83.78% | 150.00 | 2.50% | 0.00% | 8.73 |
| Stung Treng | 78.79% | 50.00 | 2.50% | 0.00% | 8.66 |
| Takeo | 86.49% | 200.00 | 10.00% | 0.00% | 8.23 |
| Sihanoukville | 91.67% | 30.00 | 11.54% | 1.92% | 7.89 |
| Pursat | 86.11% | 600.00 | 2.50% | 0.00% | 7.85 |
| Kep | 97.14% | 1025.00 | 2.50% | 0.00% | 7.56 |
| Siem Reap | 73.61% | 100.00 | 5.75% | 1.15% | 7.44 |
| Kampong Speu | 70.27% | 200.00 | 7.50% | 0.00% | 7.43 |
| Kandal | 60.00% | 75.00 | 3.85% | 0.00% | 7.36 |
| Svay Rieng | 89.80% | 60.00 | 19.23% | 1.92% | 7.14 |
| Kratie | 82.86% | 45.00 | 12.50% | 2.50% | 6.98 |
| Kampong Chhnang | 76.92% | 150.00 | 9.43% | 1.89% | 6.90 |
| Banteay Meanchey | 76.00% | 150.00 | 9.62% | 3.85% | 5.90 |
| Rattanakiri | 65.63% | 150.00 | 12.50% | 2.50% | 5.70 |
| Phnom Penh | 75.00% | 200.00 | 30.43% | 0.72% | 5.68 |
| Battambang | 79.27% | 100.00 | 11.76% | 4.71% | 5.64 |
| *Scores are re-scaled between 1 and 10 | | | | | |
| Ω: Firms answering Don't Know had their answers re-coded to Yes, so that either firms did or not experience a robbery. | | | | | |

“I just give them some money for lunch when they come to collect taxes or do inspection instead of paying the tax. If I pay the tax, it won’t go to the government account anyway, so I just give some money to the tax officials instead of paying the full tax. But if I believed the tax collection would go to government accounts, I would be more willing to pay.”

Provincial tax officials sometimes encourage this deception by offering entrepreneurs a “personal or sentimental discount” in exchange for free samples or service fees. Sometimes, they even provide these discounts based on familial relationships, as a steel window producer in Stung Treng explained:

“Actually, I pay much lower tax compared to other business like mine. I have got this special offer from tax officials because of my brother’s official title when I first started my business. At that time my brother was a high level civil servant. I was told by the tax officials not to reveal my actual tax payment to other business owners.”

For unconnected and law-abiding firms, who now must pay a higher burden to subsidize lost revenue, the tax burden can be painful. A firm in Ratanakiri was particularly vocal about the lack of equity and its costs:

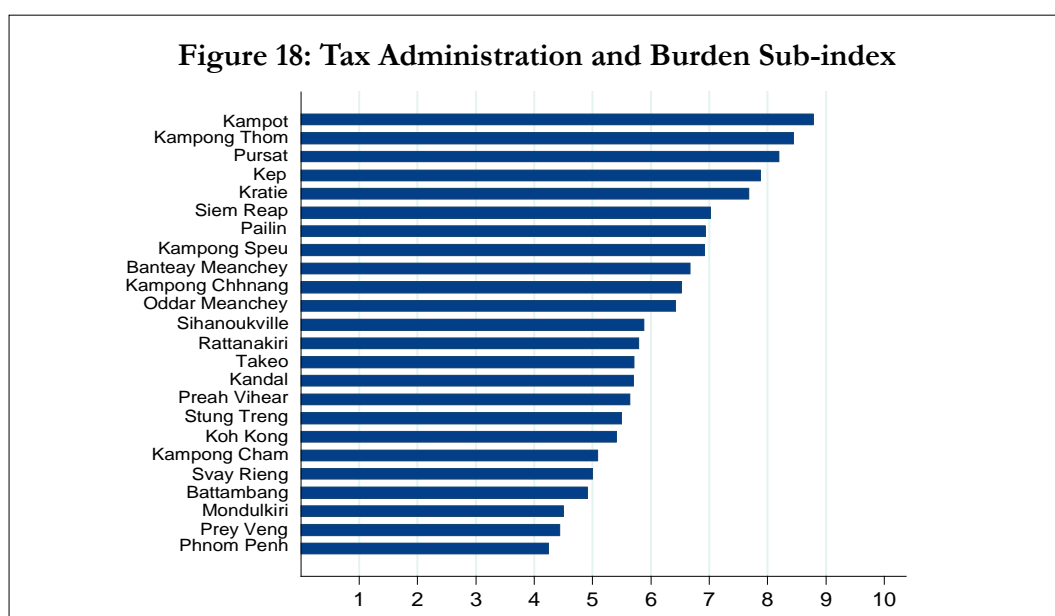
“I have a lot of problems with the tax rate charged by the tax officials. I have never seen the official tax rates issued by the government. I have paid patent tax 50% higher compared to other enterprises like mine. Moreover, I have to pay an additional 5,000 Riels to the monthly tax receipt of 10,000 Riels. Although I am upset about this, I still agree to pay them because I don’t want to have any problem with provincial authorities”

The Ratanakiri firm went on to explain that transparency was the only solution. “I think the government, especially the tax department, should publicly distribute the tax rate information to all business owners.”

To capture these taxation issues at the provincial level, the PBES research team developed a Sub-index entitled Tax Administration and Burden that includes six indicators:

1. *The percentage of firms in each province that do not pay any taxes*
 2. *The percentage of firms that view bribes paid to public officials for avoiding taxes as an obstacle to their business.*
 3. *The percentage of firms that pay bribes to provincial tax authorities to expedite the tax collection process.*
 4. *The percentage of firms that agree or strongly agree that negotiations with the tax authority are an essential part of doing business.*
 5. *The percentage of firms that believe Tax Administration imposes obstacles.*
 6. *The percentage of firms that believe Tax Burden imposes obstacles*
- *The percentage of firms in each province that do not pay any taxes.* While Cambodian firms are legally subject to a number of different taxes, including VAT, salary taxes, and excise taxes, it is profit (turnover) taxes that vary most at the provincial level. All three legal categories of profit tax rates (described in Table 24) are represented in our sample. While there are only 4% of “real regime members” (see Table 24 for a definition) in the entire sample, 17.5% in Pailin fit in this category. In Sihanoukville province, 70% of firms pay the estimated tax, a figure that is one standard deviation greater than the entire sample mean. Other provinces have been less diligent about registering their firms for profit taxes. Seventy-two percent of firms in Prey Veng and 55.2% of firms Siem Reap do not pay any taxes at all. As a result, the percentage of firms that do not pay any taxes serves as a useful indicator of the capacity of provincial tax authorities.

The next three indicators capture the arbitrary nature of tax collection at the provincial level



for all types of taxes, including profit taxes, VAT and the tax payment negotiations that firms must have with tax authorities:

- *The percentage of firms that view bribes paid to public officials for avoiding taxes as an obstacle to their business.*
- *The percentage of firms that pay bribes to provincial tax authorities to expedite the tax collection process.* In some provinces, firms may face additional fines for not paying taxes on time even though the timing of tax collection rests with tax officials. Such businesses have

taken it upon themselves to accelerate the collection process with extra payments.

- *The percentage of firms that agree or strongly agree that negotiations with the tax authority are an essential part of doing business.* While the “estimated regime” (see Table 24 for a definition) legally requires an estimated sales value, negotiations can yield a lower tax burden in exchange for informal payments. The final two indicators were taken directly from the ICA questions on obstacles to business performance. The two indicators are:

Table 24: Profit Tax Categories for Private Firms

| Level | Description | Key Documents Required | Representation in PBES Samples | |
|-------|-------------------------|--|--------------------------------|------------------|
| | | | 2009 Full | 2009 Original 10 |
| 1 | <i>Real Regime</i> | Firms with annual turnover over KR 500 million and service sector enterprises with over KR 250 million are required to file financial statements with the Tax Department of the Ministry of Economics and Finance. Any firm supplying goods or services to the government is also required to enter this regime. This tax category is known as the real regime, which necessitates a tax license, Patent tax registration, and commercial registration with the MOC. | 3.7% | 4.3% |
| 2 | <i>Estimated Regime</i> | Firms whose turnover is too small for the real regime, enter the Estimated Regime, where taxes are determined based on the estimates of enterprise sales made by provincial Tax Departments. These are typically monthly lump-sum payments determined through a negotiating process. | 33.1% | 32.9% |
| 3 | <i>Patent Tax</i> | Unregistered firms with the Provincial/Municipal Commerce Division pay an initial Patent tax but do not pay profit taxes. | 27.5% | 23.1% |
| 4 | <i>No Taxes at all</i> | | 35.7% | 39.7% |

- *The percentage of firms that believe Tax Administration imposes obstacles.*
- *The percentage of firms that believe Tax Burden imposes obstacles (interpreted as the amount paid).* While these figures generated statistically significant differences, it is interesting to note that no provinces have a mean score greater than 3, which is defined as a moderate obstacle.

Table 25 shows that firms in Kampot, for the second year in a row, and Kampong Thom suffer the least from the burden imposed by the Provincial Authority, while firms in Phnom Penh, for the second year in a row, and Prey Veng consider the Tax Authority their biggest problem.

5.9 Proactivity of Provincial Authorities

Legal ambiguity, which results from unclear wording in legal documents, delays in the promulgation of implementing documents related to national laws; and inconsistencies between implementing documents and the national laws themselves, is a standard part of doing business in Cambodia. In addition, a clear legal regime is lacking for many emerging industries. When legal ambiguity is a factor in delays, a provincial government’s choices can greatly affect the success of a business venture. Provincial officials can cost businesses considerable time and money by forcing them to wait for clarification through subsequent implementing documents or an appeal to national authorities. In a few provinces, officials

Table 25 : Indicators Comprising Tax Sub-index

| Province | Firms not paying any taxes (%) | Bribes to officials are an obstacle to business (%) | Firms negotiating with Tax Authority (%) | Tax burden as obstacle (Mean) | Tax administration as obstacle (Mean) | Tax Sub-index Score * |
|------------------|--------------------------------|---|--|-------------------------------|---------------------------------------|-----------------------|
| Kampot | 23.08% | 67.50% | 25.00% | 1.92% | 5.77% | 8.79 |
| Kampong Thom | 27.50% | 62.07% | 31.03% | 0.00% | 12.50% | 8.44 |
| Pursat | 30.00% | 53.57% | 57.14% | 5.00% | 5.00% | 8.20 |
| Kep | 27.50% | 79.31% | 41.38% | 0.00% | 2.50% | 7.88 |
| Kratie | 15.00% | 52.94% | 64.71% | 7.50% | 17.50% | 7.68 |
| Siem Reap | 55.17% | 58.97% | 53.85% | 3.45% | 10.34% | 7.01 |
| Pailin | 15.00% | 82.35% | 61.76% | 7.50% | 7.50% | 6.93 |
| Kampong Speu | 25.00% | 86.67% | 43.33% | 5.00% | 10.00% | 6.91 |
| Banteay Meanchey | 48.08% | 62.96% | 37.04% | 11.54% | 19.23% | 6.68 |
| Kampong Chhnang | 39.62% | 65.63% | 53.13% | 15.09% | 13.21% | 6.53 |
| Oddar Meanchey | 37.50% | 60.00% | 72.00% | 7.50% | 17.50% | 6.42 |
| Sihanoukville | 25.00% | 89.74% | 53.85% | 13.46% | 13.46% | 5.89 |
| Rattanakiri | 22.50% | 74.19% | 87.10% | 7.50% | 17.50% | 5.79 |
| Takeo | 42.50% | 78.26% | 65.22% | 5.00% | 17.50% | 5.71 |
| Kandal | 48.08% | 74.07% | 44.44% | 19.23% | 17.31% | 5.70 |
| Preah Vihear | 32.50% | 70.37% | 70.37% | 12.50% | 22.50% | 5.63 |
| Stung Treng | 20.00% | 78.13% | 56.25% | 10.00% | 35.00% | 5.49 |
| Koh Kong | 45.00% | 86.36% | 59.09% | 17.50% | 7.50% | 5.41 |
| Kampong Cham | 36.54% | 81.82% | 78.79% | 15.38% | 13.46% | 5.09 |
| Svay Rieng | 28.85% | 86.49% | 78.38% | 3.85% | 25.00% | 5.00 |
| Battambang | 31.76% | 81.03% | 58.62% | 14.12% | 31.76% | 4.91 |
| Mondulkiri | 22.50% | 64.52% | 77.42% | 40.00% | 27.50% | 4.51 |
| Prey Veng | 71.79% | 90.91% | 36.36% | 20.51% | 15.38% | 4.43 |
| Phnom Penh | 45.65% | 77.33% | 66.67% | 24.64% | 26.09% | 4.25 |

*Scores are re-scaled between 1 and 10

may even use such uncertainty to prevent firms from competing with their preferred local champions. Given these problems, those provincial governments that are creative and clever in their application of national law can greatly assist businesses. Similarly, officials with a knack for crafting proactive provincial initiatives that resolve problems facing firms can have a major impact on private sector development.

Most entrepreneurs understand the benefits of proactive leadership and hope their officials exemplify it. A small-sized steel window manufacturer in Kratie provinces articulated his exasperation with the lack of dynamism of his provincial leaders this way. “In my province, the provincial officials are not supportive of business activities because they have never cared about us. They never visit or invite us to talk about our business environment.”

Interviews revealed that firms’ attitudes regarding the helpfulness of Cambodian

provincial governments in ambiguous situations are generally negative. Like the owner in Kratie, a common refrain of businesspeople was, “they ignore our problems,” which was then often followed by a monologue on problems in the firm’s specific sector. Only in Kampong Cham did firms indicate any satisfaction with their government’s initiatives, particularly with major improvements in safety and security. Six indicators were used to determine the extent of provincial dynamism. The results are depicted in Table 26.

1. *Percentage of firms that regard their provincial government’s attitude toward private business as positive.*
2. *Percentage of firms that believe that their provincial government will interpret in their favor if there is ambiguity in national regulations.*
3. *Percentage of firms that believe that their provincial officials know enough about current national laws to resolve their problems by finding opportunities within those laws.*

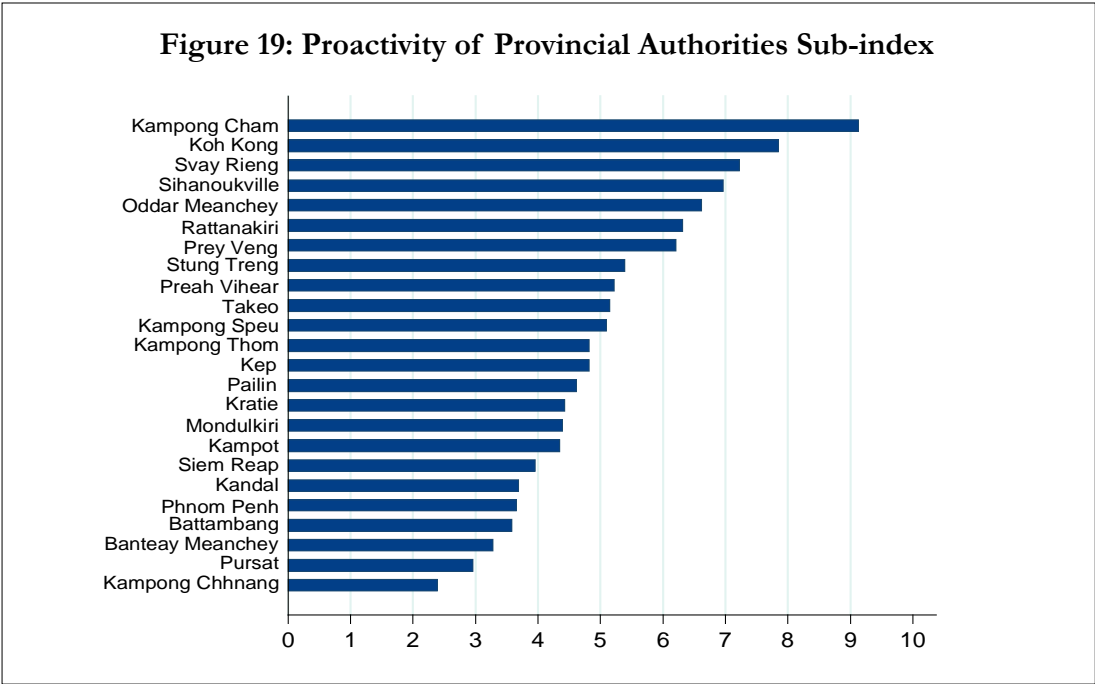


Table 26: Indicators Comprising Proactivity Sub-index

| Province | Positive attitude toward private sector (%) | In case of ambiguity, provincial government finds in firms' favor (%) | Government good at working within national laws (%) | Government creative and clever about solving firms' problems (%) | Government willing to risk punishment to assist private firms (%) | All policies come from national government (% Disagree) | Proactivity Sub-index |
|------------------|---|---|---|--|---|---|-----------------------|
| Kampong Cham | 53.85% | 46.15% | 73.08% | 67.31% | 46.15% | 57.69% | 9.14 |
| Koh Kong | 42.50% | 47.50% | 70.00% | 65.00% | 40.00% | 45.00% | 7.86 |
| Svay Rieng | 57.69% | 9.62% | 71.15% | 63.46% | 50.00% | 36.54% | 7.22 |
| Sihanoukville | 50.00% | 23.08% | 65.38% | 61.54% | 48.08% | 36.54% | 6.98 |
| Oddar Meanchey | 50.00% | 12.50% | 65.00% | 72.50% | 42.50% | 32.50% | 6.62 |
| Rattanakiri | 40.00% | 17.50% | 77.50% | 57.50% | 50.00% | 15.00% | 6.32 |
| Prey Veng | 41.03% | 12.82% | 61.54% | 58.97% | 51.28% | 38.46% | 6.22 |
| Stung Treng | 42.50% | 25.00% | 60.00% | 55.00% | 47.50% | 10.00% | 5.39 |
| Preah Vihear | 42.50% | 15.00% | 65.00% | 52.50% | 35.00% | 30.00% | 5.22 |
| Takeo | 45.00% | 20.00% | 67.50% | 55.00% | 25.00% | 27.50% | 5.15 |
| Kampong Speu | 50.00% | 12.50% | 65.00% | 57.50% | 20.00% | 37.50% | 5.10 |
| Kampong Thom | 50.00% | 12.50% | 72.50% | 40.00% | 22.50% | 35.00% | 4.83 |
| Kep | 47.50% | 15.00% | 60.00% | 55.00% | 25.00% | 32.50% | 4.83 |
| Pailin | 37.50% | 10.00% | 57.50% | 50.00% | 30.00% | 45.00% | 4.61 |
| Kratie | 50.00% | 7.50% | 57.50% | 35.00% | 30.00% | 47.50% | 4.42 |
| Mondulkiri | 35.00% | 12.50% | 62.50% | 45.00% | 32.50% | 32.50% | 4.40 |
| Kampot | 38.46% | 9.62% | 61.54% | 55.77% | 26.92% | 26.92% | 4.35 |
| Siem Reap | 36.78% | 13.79% | 55.17% | 48.28% | 26.44% | 32.18% | 3.96 |
| Kandal | 26.92% | 17.31% | 53.85% | 51.92% | 30.77% | 21.15% | 3.69 |
| Phnom Penh | 32.61% | 17.39% | 48.55% | 52.90% | 31.88% | 19.57% | 3.65 |
| Battambang | 28.24% | 12.94% | 63.53% | 47.06% | 20.00% | 28.24% | 3.59 |
| Banteay Meanchey | 13.46% | 5.77% | 51.92% | 48.08% | 30.77% | 44.23% | 3.29 |
| Pursat | 27.50% | 7.50% | 60.00% | 50.00% | 20.00% | 17.50% | 2.97 |
| Kampong Chhnang | 20.75% | 9.43% | 50.94% | 39.62% | 30.19% | 16.98% | 2.40 |

- 4. *Percentage of firms that believe that their provincial officials are creative and clever in applying national laws to resolve their problems.*
- 5. *Percentage of firms that believe that their provincial officials are willing to risk punishment from the national government to pass decisions that aid business.*
- 6. *Percentage of firms that disagree or strongly disagree that their provincial leadership has nothing to do with new initiatives that aid the private sector and that instead, all important policies come from the national government.*

The first indicator captures firms’ perceptions regarding the government’s general attitude toward private business in the province. The next

two indicators capture how well the provincial governor and provincial agencies deal with legal ambiguity. Indicators four and five measure the willingness and competence of provincial officials in resolving private firms’ problems through the existing legal framework. The final indicator simply records the proportion of firms that attribute positive business developments to the national government.

Table 26 summarizes the Proactivity of Provincial Authorities indicators. Kampong Cham ranks over a full point higher than other provinces on this aspect of economic governance. The lowest scores were recorded in Pursat and Kampong Chhnang.

5.10 Dispute Resolution

According to the 2009 ICA, the weak rule of law in Cambodia increases firms' investment risks and costs, constrains their business operations and ultimately limits their growth.²³ To resolve this problem, the ICA recommended that the functioning of the courts be improved, so that impartial and legal-based judicial decisions can underpin contracting and backstop alternative dispute resolution. The notion of backstopping alternative dispute resolution is particularly important, as few firms in any of the provinces sampled rely on the court system, due to their belief that the courts are biased and prove expensive. A firm in one province, which recently resolved a major dispute with a customer using a local mediator remarked, "I did not choose the court to solve the problem because it costs a lot of money (even more than the loan) and time."

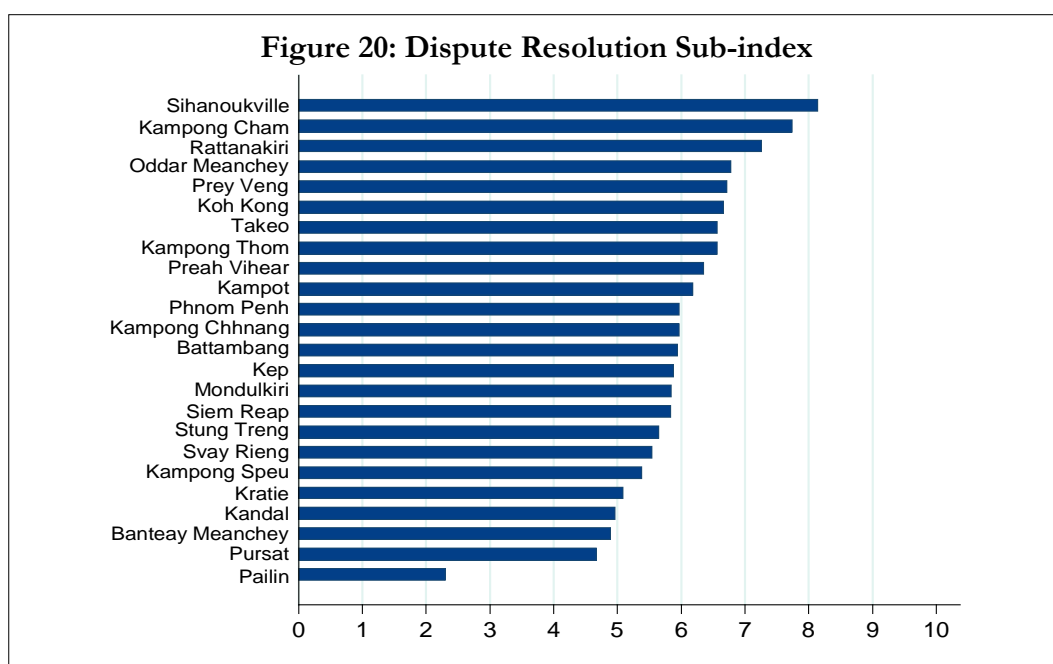
Our survey results bear out these anecdotal claims: less than 1% of firms cited provincial courts as their most common or second most common mode for resolving disputes and less than 9% chose it as their third most common

mode. Instead, firms preferred to go through independent negotiations (cited by 93% of firms as their top option), and negotiations facilitated by friends and relatives (considered by 22% of firms as their second-best option). These figures are for the 51% of firms that claimed to have had a business dispute in the past year.

Because formal modes of dispute resolution were used so infrequently, this index not only sought to capture the development of the legal system, but also included a range of indicators to measure firms' general satisfaction with any dispute resolution method, whether formal or informal.

Seven indicators assembled from questions scattered throughout the survey comprise the index. The first is:

1. *Percentage of firms agreeing that the legal system would uphold their contract and property rights in business disputes.*
2. *Percentage of firm sales that were not paid within the agreed-upon time.*
3. *Percentage of firm sales that were never repaid.*
4. *Percentage of firms able to recover money that was due to them.*



²³ World Bank and IFC. 2009: 37

5. *Percentage of firms satisfied with the method of dispute resolution that they had chosen.*
6. *Percentage of firms that said the following statement was seldom or never possible: "If a government agency acts against the rules (due to overzealous inspectors, unofficial payments, etc.), I can usually go to another official or to his superior to have the issue corrected."*
7. *Percentage of firms that answered seldom or never to the question, "Based on your observations of other cases in your province, do you believe there is a fair process for disputing changes in rent contracts?"*

The first indicator is intended to measure divergence at the provincial level in firms' perceptions of the provincial court system and its impact on property rights. The ICA found that 25% of Cambodian firms agree with this statement. The PBES, however, finds much more variance across the country, ranging from less than 2% in Banteay Meanchey to over 40% in Kampong Cham. As most businesses have never used the court system at all, it is important to remember that this is purely based on perception and has little to do with experiential understanding of the system.

Indicators two through five measure the impact of all forms of dispute resolution. Unpaid sales are an indication that firms have limited opportunities to appeal the practices of delinquent and unscrupulous customers. As a result, two questions gauge the extent of the problem and a third assesses firms' success in recovering such payments. The last question (Indicator 5) measures firms' overall satisfaction with their chosen method of dispute resolution.

Indicators six and seven measure whether there are administrative mechanisms that allow firms to appeal the actions of provincial authorities and landlords concerning changes in rental contracts.

Table 27 summarizes the scores on Dispute Resolution. Firms in Phnom Penh and Siem Reap are shown to be most satisfied with provincial dispute resolution procedures, while those in Sihanoukville are least satisfied.

Table 27: Indicators Comprising Dispute Resolution Sub-index

| Province | Percentage of sales not paid within agreed-upon time (median sales) | Percentage of sales never paid (median sales) | Legal system will uphold property rights (%) | Appeal unjust actions of provincial official (% seldom or never) ^ψ | Firms satisfied with chosen method of dispute resolution (%) | Firms successful in recovering money owed to them (%) | Dispute Resolution Sub-index |
|---|---|---|--|---|--|---|------------------------------|
| Banteay Meanchey | 5 | 2 | 1.92% | 71.15% | 54.55% | 30.95% | 4.89 |
| Battambang | 5 | 2 | 15.29% | 68.24% | 74.29% | 42.62% | 5.94 |
| Kampong Cham | 5 | 5 | 40.38% | 36.54% | 70.59% | 62.07% | 7.75 |
| Kampong Chhnang | 3 | 2 | 22.64% | 71.70% | 76.74% | 32.50% | 5.97 |
| Kampong Speu | 4 | 2 | 32.50% | 85.00% | 35.71% | 33.33% | 5.38 |
| Kampong Thom | 0 | 0 | 27.50% | 85.00% | 64.00% | 43.75% | 6.56 |
| Kampot | 0 | 1 | 17.31% | 57.69% | 50.00% | 28.57% | 6.19 |
| Kandal | 5 | 4 | 21.15% | 90.38% | 25.81% | 44.12% | 4.97 |
| Koh Kong | 10 | 5 | 37.50% | 20.00% | 68.42% | 42.86% | 6.67 |
| Kratie | 5 | 3.5 | 25.00% | 72.50% | 0.00% | 45.45% | 5.08 |
| Mondulkiri | 7 | 5 | 27.50% | 67.50% | 88.89% | 30.00% | 5.84 |
| Phnom Penh | 0 | 5 | 18.84% | 67.39% | 34.91% | 39.34% | 5.97 |
| Preah Vihear | 0 | 3.5 | 30.00% | 60.00% | 60.00% | 18.75% | 6.36 |
| Prey Veng | 1 | 1 | 38.46% | 58.97% | 60.00% | 27.78% | 6.71 |
| Pursat | 10 | 3 | 12.50% | 75.00% | 72.00% | 33.33% | 4.68 |
| Rattanakiri | 2 | 3 | 57.50% | 62.50% | 50.00% | 42.11% | 7.27 |
| Siem Reap | 1.5 | 1 | 24.14% | 78.16% | 42.42% | 33.33% | 5.84 |
| Sihanoukville | 1.5 | 2 | 42.31% | 51.92% | 60.87% | 71.43% | 8.14 |
| Stung Treng | 5 | 2 | 35.00% | 77.50% | 40.00% | 38.10% | 5.64 |
| Svay Rieng | 7 | 2.5 | 32.69% | 63.46% | 53.13% | 46.15% | 5.54 |
| Takeo | 2 | 4 | 40.00% | 70.00% | 55.00% | 36.84% | 6.57 |
| Oddar Meanchey | 2.5 | 2 | 25.00% | 57.50% | 100.00% | 28.57% | 6.78 |
| Kep | 3 | 1 | 12.50% | 75.00% | 33.33% | 59.09% | 5.88 |
| Pailin | 20 | 5 | 17.50% | 95.00% | 50.00% | 23.33% | 2.30 |
| *The Dispute Resolution Sub-index is the mean of all seven indicators after re-scaling to a 10-Point Scale. | | | | | | | |
| ^ψ The only 2 "Don't Know" responses were recoded to the neutral answer of Sometimes. | | | | | | | |

6. Changes in Key Indicators between the 2006 and 2009 PBES

In this section of the report, we study how the Cambodian business environment has changed over time, highlighting areas of clear policy successes and policy areas where more work is necessary. To assure comparability, we base our analysis on the original ten provinces surveyed in the 2006 PBES. Section 6 focuses on repeated cross-sections of firms, meaning that different firms answered the survey in 2006 and 2009 PBES. In comparing these two groups, it is important to remember that we are not asking how individual businesses experienced changes in the business environment over time, but on the aggregate responses between the two groups. These results offer useful insights, but

also pose some puzzles. As a result, in Section 7 we supplement this analysis with results from the PBES panel respondents of 152 firms who answered in 2006 and 2009 PBES.

Table 28 summarizes the results. Upward arrows represent positive changes, downward negative, and sideways arrows represent ambiguous developments.

6.1 Improvements in the Business Environment

Entry Costs: Entry costs appear to have improved generally across the country. In addition to the provinces that have implemented an OWS for registration procedures since the last PBES, we can also see that the total number of documents required in order to become fully legal has declined (down from 5 to 4). The total number of days for business registration at the Provincial Department of Commerce has also declined (down from 20 to 16.75 days), and the time required to pay the Patent Tax for very small operations is considerably lower too (down from 15 to 12.25 days). The one exception to this general trend is the time required to obtain a one-year operating license, which has actually increased somewhat. Formal fees for business documentation have also increased, but their increase is far below the rate of inflation recorded over the same period.²⁴

| Table 28: Summary of Changes in Sub-index Performance Between 2006 & 2009 | |
|---|------------------|
| Index | Change Direction |
| Entry Procedures | ↑ |
| Property Rights | ↑ |
| Transparency | → |
| Time Costs of Regulation | ↑ |
| Informal Charges | ↓ |
| Participation | → |
| Crime Prevention | → |
| Taxes | ↑ |
| Proactivity | → |
| Dispute Resolution | ↓ |

²⁴ Fees for business documentation include formal and informal fees that business owners have paid to obtain formal documents for starting up a business.

Property Rights: Property rights demonstrate some improvement. More firms in the median province have some form of property documentation (87% to 96%). Of those, the number with a formal title has increased about 10 percentage points (59% to 69%). In addition, expropriation risk has declined from 4.5% in the median province to 3%. These improvements bode well for business development and investment. The story isn't entirely perfect, however, particularly for those renting or looking to purchase land. On the negative side, violations in rental contracts has increased and land continues to be overvalued according to our measure of effective price.

Time Costs of Regulatory Compliance: Regulatory procedures show some sign of easing. While firms do report spending more of their time on bureaucratic procedures, the median²⁵ number of business inspections has declined (from four to two times per year) and waiting periods for new land for existing businesses has been cut in half from 58 to 30 days.

Tax Administration: Some improvement in tax administration is also apparent. Fewer firms negotiate their final payment with provincial authorities (64% on average in 2006, compared to 54% in 2009) and consequently fewer owners complain that paying bribes to lower taxes are a problem (80% down to 75%). Of course, these are only marginal improvements. Seventy-five percent of businesses still consider that bribes to the tax authority are an obstacle to business operations. This amount is a very high proportion by international standards. In addition, more firms cited frustration with tax rates and tax administration. This shows that there is much more work to be done to construct a fair and equitable tax system that appropriately taxes firms for government services, but is not so prohibitive that it handicaps their ability to

conduct business. It is notable that the number of firms not paying any taxes at all has nearly doubled in the past two years. In part, this may be a reflection of the youth and informality of new operations, but it could also be, in part, a reaction to a tax system that many business owners believe is unfair. This has negative consequences for national and provincial governments because they are deprived of important revenue they could use to improve infrastructure and social services.

6.2 Ambiguous Change in Key Areas

Transparency: Transparency of business documentation shows mixed results. While there has been some improvement on key indicators since 2006, they still represent low transparency by international comparisons. Access to basic documentation has improved, but 54% of firms still say that it is impossible to access the provincial budget, while 26% say it is very difficult. When it comes to land allocation and infrastructure maps, the numbers are 37% and 31% claiming access is impossible, and 30% and 32% answering very difficult. Where access has improved, it has been on less critical information such as operating license and registration application.

Knowledge about business documentation has improved. In 2006, 58% were unaware of provincial budgets. In 2009, however, only 20% of businesses in the median province were not sure what a provincial budget was. On other documentation, improvement has been even more dramatic. There is no longer a single document with awareness lower than 65%, whereas in 2006 every document was below that threshold.

Equity of access and predictability also show slight improvements, but remain very low. In

²⁵ The median is the middle value in a list of numbers.

total, 73% of businesses claim to be uninformed about changes in laws that materially affect their businesses. This is down from 82% in 2006, but still extremely high. Fifty-five percent of businesses in the median province believe some sort of relationship is necessary with provincial authorities to get such documentation. Furthermore, 47% believe there is overt favoritism toward politically-connected firms.

It has been said before, but it bears repeating: transparency is critical for small businesses. The more information they have, the better they can forecast business prospects and risk. This allows them to make educated decisions about investment and expansion. Without such information, firms avoid expansion for fear of experiencing unanticipated problems due to changes in laws and other factors that impact the business climate. Access to clear and reliable information about regulations, legal fees and taxes not only make business-owners more responsible, but also less vulnerable to arbitrary decisions. Furthermore, transparency is among the easiest policy choices to make. It is far easier to increase access to information than to change provincial institutions. Provincial officials who are seeking a short-term boost in their province's PBES score would benefit from simply making information available in the lobbies of the provincial agencies where business owners go to seek information.

Participation: Participation also remains level. More firms believe they are consulted for advice on legal changes, but the proportion is still only 3.8% of entrepreneurs. Membership in business associations has grown only from 1.3% of sampled firms to 1.9%. Finally, there was very little evidence of mechanisms for connecting firms to policy-makers. The median province held only 2.5 business forums per year (the highest province held 21) and the majority of firms did not have suggestion boxes available in district offices.

Crime: Exposure to crime has not changed very much over time. In 2006, 30% of firms in the median province were victims of theft or arson. Although the number of victims has now dropped to 22%, the cost of these crimes has risen. In the median province, firms suffered an average monetary damage of \$100 from criminal behavior. Protection payments have also not improved very much. In 2006, 11% of firms made such payments; now 9.5% admit to the behavior. A small reduction, but well within the 3% sampling error.

Proactivity: Proactivity scores have hardly budged. The dynamism of provincial leaders remains almost exactly the same as in 2006. For instance, in 2006, 36.3% of firms ranked the attitude of officials as positive; in 2009, the number was 34.7%. Similarly, in 2006, 57.5% of firms in the median province answered that their local leaders were creative about working within national laws to create a positive business environment. In 2009, the number of those agreeing their provincial officials were creative was 58.4%.

6.3 Declines in Key Areas

The 2009 PBES also captures some deterioration in the business environment. Some of these indicators are critically important and should be given immediate attention by local, provincial, and national officials.

Informal Charges: Informal Charges appear to have worsened slightly. In the 2009 PBES, only 52% of businesses denied paying bribes to provincial officials, down from 56% in the 2006 PBES. Moreover, there has been an 8% increase in the number of businesses reporting that corruption is an obstacle to their business (now 42% in the median province). Most strikingly, 31% of businesses report that if they pay one bribe, additional agencies are also likely to visit them and ask for bribes. In 2006,

only 17% of businesses in the median province reported this multiplier effect. While public procurement has improved marginally, much more improvement needs to take place. Only 19% of firms in the median province believe that there is sufficient and transparent information on public procurement contracts, while 62% of businesses in the median province believe that personal connections are necessary to win a bid. Moreover, 75% of businesses believe 'kick backs' are regularly required to win government contracts.

Dispute Resolution: Dispute resolution shows significant decline as well. Most importantly, entrepreneurs report less confidence in formal institutions. Only 22% of firms in the median province believe that the legal system will protect their property rights; down from 34% in 2006.

Correspondingly, only 41% of respondents were satisfied with resolution of their

contractual disputes over the past year, and 65% of businesses were not successful in recovering payments owed to them by delinquent clients.

In 2006, 53% of businesses were unsuccessful in recovering monies owing to them. These findings are worrisome. First of all, the scale of unpaid bills is equal to about 2.8% of total sales, so poor dispute resolution is costing businesses a great deal of money. Secondly, as more businesses join the market and as Cambodia further integrates internationally, formal means of dispute resolution will become even more critical. Businesses will no longer be able to rely on social relations, provincial leaders, and other informal measures to enforce contracts, as they will be doing a greater proportion of business with firms outside their social networks. The lack of confidence in formal means of dispute resolution raises the risk of doing business and has the potential to limit business expansion and growth.

7. Panel Analysis

Taking advantage of the fact that the PBES survey has now been conducted twice over the last four years, a panel group of 152 respondents was selected from the 2006 survey and asked the same questions again to measure changes of their perceptions over time.

Since the last PBES in 2006, Cambodia has embarked on major endeavors to improve land titling, through the Land Mapping and Administration Project (LMAP) and expedite business registration through the implementation of the 2005 Commercial Law and One Window Service in strategic provinces. Moreover, the economy has experienced a tremendous boom in 2007 and dramatic slowdown in 2008. Evaluating the success of these endeavors and impact of other changes in the business environment since 2006 is difficult in a traditional survey setting that relies on completely separate random samples of businesses in each iteration (known as repeated cross-sections). Normal sampling error and changes in the underlying population of firms over time (e.g. the dramatic growth in new businesses over the past two year uncovered by our business listing) can create difficulties in truly understanding the causal implications of changes in government regulations or the macro-economy. We can never be absolutely certain that we are comparing apples to apples.

To address this deficiency, the PBES research team supplemented our cross-sectional analysis in Section 6 with a special random sample

of 152 panel respondents, who answered in the 2006 and 2009 PBES. Because these respondents run exactly the same businesses and have exactly the same personality and demographic characteristics as before, they provide a very reliable source of information in how changes in the business environment have affected business perceptions and behavior. As with a panel analysis in a public health setting, we can set aside confounding differences in the construction of our sample and focus directly on changes in this group over time. A close look at this data can provide important insights into the Cambodian economy today.

7.1 Business Confidence and Growth

We begin with an analysis of how expectations of the future of their businesses have changed. Table 29 shows four columns. The first two columns depict the perceptions of the 152 firms in the PBES sample in 2006 and 2009. Because PBES sampling is designed to reflect provincial populations of businesses, it can be misleading to draw general conclusions about the national economy. After all, Phnom Penh and Battambang comprise 45% and 10% of the firms in Cambodia nationally, but only 18% and 13% of the PBES panel sample. To derive a nationally representative sample, which accounts for the concentration of businesses in Phnom Penh, we re-weight the analysis by the percentage of businesses in each province from the PBES listing. These results are displayed in columns 3 and 4 of Table 29.

In both cases, the results are striking. Businesses throughout the country, and particularly in Phnom Penh, are much less confident about their business prospects. Enterprises are about 12% less likely to have an interest in expanding their business. Moreover, almost 4% more operations are considering closing. These results reflect the wariness firms felt in October 2008 when the survey was conducted. Cambodia was experiencing the effects of inflation, especially in fuel and land costs. Nevertheless, the survey proceeded before the global financial crisis hit Cambodia.

It is not just business confidence that has declined over time either. Actual size (measured by average employment) is down over the last

three years as well. Most of the labor shedding has taken place among firms in the middle two size groupings. These firms have retreated to the size of two full-time employees or less. There has been some compensation for the decline in permanent employment through the hiring of more seasonal labor, but the total increase in seasonal labor is still quite small.

Many entrepreneurs blame their poor business prospects on provincial officials. There has been a significant decline in the reported attitudes of provincial officials over time. Ratings of officials as positive dropped 7% in the PBES sample and 19.55 in the nationally weighted sample. This helps explain the general decline in PBES scores between the two years.

Table 29: Change in Panel Respondent’s Business Expectations

| Plans over Next Two Years | PBES Sample | | Nationally Representative | |
|--|-------------|-------|---------------------------|-------|
| | 2006 | 2009 | 2006 | 2009 |
| Increase Size of Operations Considerably | 23.7% | 19.1% | 28.4% | 17.4% |
| Increase Size of Operations | 36.2% | 32.1% | 34.2% | 33.3% |
| Continue Operating at Present Size | 35.5% | 41.5% | 35.3% | 43.6% |
| Reduce Size of Operations | 3.3% | 3.3% | 1.5% | 1.6% |
| Reduce Size of Operations Considerably | 0.7% | 0.7% | 0.5% | 0.2% |
| Plan to Close this Business | 0.7% | 2.6% | 0.2% | 3.9% |

Table 30: Change in Business Size

| Size of Firm (Number of Employees) | PBES Sample | | Nationally Representative | |
|------------------------------------|-------------|-------------|---------------------------|--------------|
| | 2006 | 2009 | 2006 | 2009 |
| 2 or less | 35.5% | 54.6% | 31.0% | 56.5% |
| Between 3 and 5 | 44.1% | 27.0% | 45.5% | 27.0% |
| Between 6 and 10 | 15.8% | 12.5% | 17.0% | 9.0% |
| Between 11 and 30 | 4.6% | 5.9% | 6.5% | 7.5% |
| More than 30 | 0.0% | 0.0% | 0.0% | 0.0% |
| <i>Percent Seasonal</i> | <i>3.1%</i> | <i>5.2%</i> | <i>3.60%</i> | <i>4.10%</i> |

Table 31: Change in Attitude of Provincial Officials

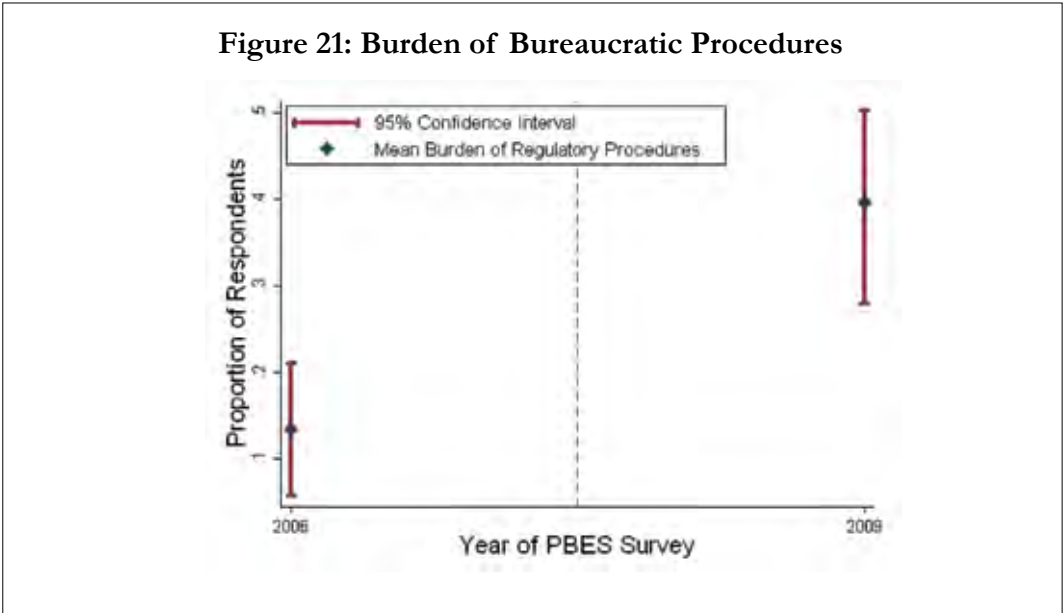
| Attitude of Provincial Officials | PBES Sample | | Nationally Representative | |
|----------------------------------|-------------|-------|---------------------------|-------|
| | 2006 | 2009 | 2006 | 2009 |
| Very Negative/Negative | 21.7% | 19.7% | 10.7% | 21.4% |
| Neutral | 32.2% | 41.5% | 33.5% | 42.3% |
| Very Positive/Positive | 46.1% | 38.8% | 55.8% | 36.3% |

Why do firms believe the attitude of officials has declined? A number of factors point to clear and statistically significant improvements in official behavior according to panel firms. More of the panel firms deny paying bribes to provincial officials in 2006 and 2009 (48% or 57%); fewer firms report protection payments to provincial police officers (15% to 8%); median inspections of businesses have declined from 6 to 2; and less respondents were victimized by crime in the last year (33% to 20%). Moreover, information access has improved for this group of older firms. Firms are more likely to have access to important business documentation (including laws and land maps). In 2006, only 1% of panel respondents reported that they were informed about changes in laws, which materially affected their business. By 2009, the number had grown to 12.5, still a relatively small number, but a dramatic jump over previous years. It is interesting that access to information is so different between panel firms and the larger cross-section. In part, the greater access to business information may result from their greater knowledge of where to look for information and their experience working with provincial officials over time.

The one factor that shows statistically significant declines over time is the burden that panel firms are spending on bureaucratic procedures. As Figure 21 shows, in 2006, only 13% of businesses spent 15 days annually on government formalities. In 2009, over 39% of businesses spent over 15 days dealing with government regulations and interacting with officials.

7.2 Business Formalization

What about the formalization puzzle? Cambodian officials have made great strides to ease the burden and monetary cost of formal registration and a few provinces have begun experimenting with OWS registration and licensing. A brief look at the cross-sectional data appears to indicate that these policies have not been followed by improvement in business formalization. Our analysis of formalization in the original ten provinces that answered the 2006 PBES reveals that the number of businesses without any documentation at all has increased from 16% to 40%. Since these results from the same listing and stratified random sampling approach, one might imagine that two numbers



are directly comparable and that there has been a dramatic increase in informality between the two surveys. Afraid of the poor economy or government intervention, firms might be choosing not to renew their documentation and function at a greater distance from the oversight of officials.

However, the conclusion that these policies have failed appears incorrect. Increased informality in the general Cambodian business environment is a function of the much younger population of businesses in Cambodia. Rapid economic growth fueled the dreams of new entrepreneurs, who have started businesses at a dramatic clip. Forty-two percent are less than two years old, while another 22% are less than five years old. This result has critical implications for our analysis. This rapid growth of new start-ups in the past few years has meant that many firms have only just begun operations, and have not yet fully formalized their activities.

But what about older establishments, have they been more or less likely to formalize their establishments? The Ministry of Commerce simplification and the OWS procedures in Siem Reap and Battambang were instituted between the two surveys and therefore provide an excellent opportunity for us to test their effects using the panel data.

Table 32 reveals our findings that, in fact, there has been an improvement in registration over time. Nine percent of firms in the total PBES sample sought formal registration at either the Ministry or Provincial Department of Commerce between the two surveys. There has also been an increase in the number of firms moving from no documentation at all to paying their annual patent tax to the provincial tax authority. Interestingly, slightly less firms have operating licenses from the line department governing their business sector. This finding reflects some confusion among businesses about the need for both registration certificates from the provincial department commerce and an operating license from the same department when they operate in the retail or trading sector.

An alternative gauge of formalization is the percentage of firms not paying any taxes at all, including taxes under the real regime, estimated profit taxes, and patent taxes. This proportion for firms has fallen over time across the country. The most precipitous decline is in Phnom Penh, which is why the nationally representative survey shows a 13-point fall from 41% untaxed operations in 2006.

Table 32 : Change in Business Formalization

| Documentation/Formality | PBES Sample | | Nationally Representative | |
|--|--------------|--------------|---------------------------|--------------|
| | 2006 | 2009 | 2006 | 2009 |
| National-Level Registration | 2.0% | 3.3% | 0.78% | 6.6% |
| Provincial-Level Registration | 34.2% | 42.1% | 22.13% | 21.2% |
| Three-Year Operating License | 1.3% | 2.6% | 0.48% | 0.6% |
| One-Year Operating License | 33.6% | 29.6% | 26.45% | 21.2% |
| Patente Tax Receipt | 69.7% | 74.3% | 61.07% | 65.6% |
| <i>No Documentation</i> | <i>22.4%</i> | <i>21.7%</i> | <i>30.83%</i> | <i>33.0%</i> |
| <i>Firms not paying any taxes at all</i> | <i>28.3%</i> | <i>23.7%</i> | <i>41.3%</i> | <i>28.2%</i> |

7.3 Land Titling

The rigorous land-titling program underway also appears to be paying dividends. For the 84 businesses that operate on family land or land purchased from another party, official documentation of these properties has increased. Seven percent more operations have now received an official land title, providing them the highest level protection along with the ability to sell or mortgage their business premises. Four percent more have applied for a land title, but have not received it yet. These operations have so-called “soft titles” in the form of receipts that they can use to document their ownership. Soft titles, however, have less legal standing and add less value to the land when it comes to sales or use as collateral.

While these improvements are verifiable and laudable, they are small relative to what might have been expected given the size of the land-titling program in Cambodia. According to official data, over one million new titles have been issued since 2006 in the ten provinces covered by the PBES. In the ten provinces where the PBES panel survey was conducted, over one million pieces of land were subject to systematic land titling in 2008. According to LMAP data, 72% of land parcels included in the original survey of land in the eleven target provinces have now been distributed. Given that very high proportion, we should have witnessed a much higher land title acquisition rates among our panel firms. What accounts

for this discrepancy? Future research certainly needs to sort out this dilemma.

7.4 Access to Capital

It is commonly argued that greater documentation of property rights facilitates access to capital. Firms with formal land titles are thought to have greater access to bank loans, as they are more able to use their land as collateral.

This does not appear to be the case in Cambodia. There has been remarkably little change in the capital structure of firms between the two surveys. Respondents are still overwhelmingly likely to rely on retained earnings or funds from family and friends for their capital needs. Almost 96% of the investment in businesses comes from these two sources. Bank lending is very low, and although there are slightly more firms with bank loans than before, they account for a smaller share of total capital.

While it is true that 100% of the 18 firms that received bank loans were required to use their land or building as collateral, only three of the businesses actually had hard titles at the time that the land was issued. This indicates that Cambodian banks place particularly strong weight on land documentation. In fact, of the 13 firms that upgraded to hard titles between the two surveys, only 1 received a bank loan. The rest did not even apply for loans, claiming that they did not need the capital.

Table 33 : Change in Land Titling

| Documentation | PBES Sample | | Nationally Representative | |
|----------------|--------------|--------------|---------------------------|--------------|
| | 2006 | 2009 | 2006 | 2009 |
| No Title | 46.7% | 36.2% | 61.1% | 47.8% |
| Soft Title | 23.7% | 27.6% | 13.6% | 16.8% |
| Pre-2000 Title | 15.1% | 14.5% | 15.1% | 13.7% |
| Hard Title | 14.5% | 21.7% | 10.2% | 21.7% |
| <i>Renters</i> | <i>35.5%</i> | <i>36.2%</i> | <i>46.1%</i> | <i>47.8%</i> |

In fact, the lack of need for bank investment was a general phenomenon. Ninety-eight percent of the PBES panel respondents, who did not have a loan, did not apply for one. And of those who did not apply, 90% of respondents claimed that they did not need the resources, preferring to rely on retained earnings or family money. Only 5% of firms blamed bank administration/ collateral requirements and the high interest rates charged respectively.

These results are mirrored in the 2009 cross-sectional analysis as well. Only 11% of businesses in the full 2009 PBES currently have commercial bank loans. Of the remaining 89% of operations, 1,070 operations (98%) did not apply for bank funding. Of those that did not

apply, 982 (92%) claimed they did not need the loans because they were happier to rely on retained earning or friends and family for capital. This leaves 88 firms who did not apply for loans, because of cumbersome application procedures (20 businesses), collateral requirements (17), high interest rates (49), and fear of rejection (2). Thus, firms that want bank capital but cannot get it because of bureaucratic reasons are a distinct minority and it is hard to generalize about them. Nevertheless, it is worth noting that 82 of the operations scared away by bureaucratic procedures have less than six employees. Very few of the medium to large businesses in our sample believed they needed bank capital for their current business expansion plans.

Table 34 : Changes in Access to Capital

| Documentation | PBES Sample | | Nationally Representative | |
|---|-------------|--------------|---------------------------|-------------|
| | 2006 | 2009 | 2006 | 2009 |
| Internal Funds/Retained Earnings | 75.9 | 76.0 | 70.0% | 81.1% |
| Family/Friends | 16.6 | 19.6 | 25.6% | 16.5% |
| Private Commercial Bank | 3.3 | 1.5 | 1.7% | 1.4% |
| Informal Sources (Money Lenders) | 2.0 | 0.7 | 1.4% | 0.2% |
| Micro Finance Institution | 0.1 | 2.3 | 0.0% | 0.8% |
| <i>Percentage of Firms with Bank Loan</i> | <i>9.9%</i> | <i>11.8%</i> | <i>5.3%</i> | <i>6.6%</i> |

8. Methodology

This section provides a summary of the methodology used in the PBES.

8.1 Sampling and Selection

The 2009 PBES research sampling strategy consisted of three broad steps. First, a listing of MSMEs was established in the provincial capitals of each province. In provinces with substantial economic activity, an additional district was sampled from outside the provincial capital. The listing and firm-level information was used to draw a stratified random sample of businesses for closer analysis. Second, face-to-face interviews of business owners were conducted in order to capture business perceptions on key aspects of provincial economic governance. Third, focus group discussions, interviews with provincial officials and experts at the national and local level, and published data related to economic development were assembled to complement the perception data from the survey. This third step is referred to as “secondary data collection.”

8.1.1 Comprehensive Listing of Active Operations

Researchers traveled to each province to undertake a complete listing of business within three kilometers of all provincial capitals and additional sampled districts. Every business

operation in a fixed location, formal and informal, was recorded along with basic information: the location of the business, the activity, the gender of owner, the number of employees, etc. In total, **63,507 firms/establishments** were listed across Cambodia’s 24 provinces. The listing exercise is made necessary by the lack of an updated and exhaustive dataset on provincial MSMEs in Cambodia that is comparable across provinces. The data from the listing can be considered extremely reliable and representative, as the total response rate for the exercise was 95.5%. No single province had a response rate lower than 90%. Moreover, the median provincial response rate of 98.9%, with a standard deviation of 2.2%, indicates that non-response bias did not impact any province disproportionately.

8.1.2 The Survey

The listing was then used to randomly select a stratified provincial-level sample of 1,080 firms/establishments across all provinces, with the strata based on the sector and employment size of operations. For the purpose of the study, analysis was focused on growth-oriented businesses as opposed to merely subsistence-oriented operations, so all enterprises where the owner was the only permanent employee were excluded before sampling.²⁶ The median provincial response rate of initial contact

²⁶ The exception was Stung Treng, Oddar Mancheay and Preah Vihear, where the number of growth-oriented businesses was too small to support a statistically reliable sample. In this case, some single-employee companies were sampled. To maintain comparability with the other provinces, replacement firms were randomly sampled based on descending floor area size, so that larger subsistence-based businesses had a higher probability of selection.

with firms was 60%.²⁷ When a firm refused, a replacement firm was randomly selected from the list, so that target quotas for each province could be achieved. All provinces had at least 39 target respondents, but some more populous areas, such as Phnom Penh (111), Battambang (65), and Siem Reap (66) had slightly larger targets to ensure representation. Following general practices of calculating sampling error, we can assume a 4% margin of error around aggregate responses.

Table 35 depicts how stratified random sampling works in practice to mirror provincial populations. First, the comprehensive listing

identified 1,673 operations with over one full-time employee besides the owner in Siem Reap province. These operations were then divided into 15 baskets based on the sector in which the businesses operate and the number of employees. Thus, service sector businesses with less than five workers comprise 38% of operations in the province. Once these proportions were known, we determined the number of businesses we would need to sample to accurately mirror the Siem Reap population. Given that we were going to interview 66 firms, we would need 25 respondents to equal the 38% of small firms operating in the service sector. These businesses were randomly sampled from

Table 35: Stratified Random Sampling in Siem Reap

| All Firms in Siem Reap Province <i>(Total Number of Workers)</i> | | | | | | |
|--|--------|--------|---------|----------|----------|-------|
| | Total | | | | | |
| Comprehensive Listing | 1673 | | | | | |
| Population Share | 100% | | | | | |
| PBES Sample (Based on Listing) | 66 | | | | | |
| Actual PBES Sample Share | 100% | | | | | |
| Service <i>(Total Number of Workers)</i> | | | | | | |
| | Total | 1 to 5 | 6 to 10 | 11 to 20 | 21 to 30 | >30 |
| Comprehensive Listing | 897 | 639 | 136 | 53 | 24 | 45 |
| Population Share | 53.62% | 38.19% | 8.13% | 3.17% | 1.43% | 2.69% |
| PBES Sample (Based on Listing) | 35 | 25 | 5 | 2 | 2 | 2 |
| Actual PBES Sample Share | 53.03% | 37.88% | 7.58% | 3.03% | 3.03% | 3.03% |
| Manufacture <i>(Total Number of Workers)</i> | | | | | | |
| | Total | 1 to 5 | 6 to 10 | 11 to 20 | 21 to 30 | >30 |
| Comprehensive Listing | 139 | 95 | 32 | 10 | 1 | 1 |
| Population Share | 8.31% | 5.68% | 1.91% | 0.60% | 0.06% | 0.06% |
| PBES Sample (Based on Listing) | 6 | 4 | 1 | 1 | 0 | 0 |
| Actual PBES Sample Share | 9.09% | 6.06% | 1.52% | 1.52% | 0.00% | 0.00% |
| Commerce <i>(Total Number of Workers)</i> | | | | | | |
| | Total | 1 to 5 | 6 to 10 | 11 to 20 | 21 to 30 | >30 |
| Comprehensive Listing | 637 | 592 | 27 | 14 | 3 | 1 |
| Population Share | 38.08% | 35.39% | 1.61% | 0.84% | 0.18% | 0.06% |
| PBES Sample (Based on Listing) | 25 | 23 | 1 | 1 | 0 | 0 |
| Actual PBES Sample Share | 37.88% | 34.85% | 1.52% | 1.52% | 0.00% | 0.00% |

²⁷ The response is not perfect, but is extremely high for business surveys in general, especially developing countries. Given the sensitive nature of the instrument and the fact that many firms were answering such questions for the very first time, the response rate is very impressive. Please note, however, that response rates were significantly reduced in provinces affected by the Preah Vihear border conflict. Bateay Meanchey (33%), Battambang (43%), Order Meanchey (39%), and Preah Vihear (29%) all had below average responses. Robustness testing indicated that low response rates did not impact final PBES rankings.

the 639 operations that fit this category. We repeated this exercise for each of the 15 baskets of operations in each province.

Consequently, our sample can be considered an exceedingly accurate representation of the type and size of businesses in each province.

In face-to-face interviews, business owners were asked more than 60 questions regarding their perceptions of their business environment. Covering all 10 sub-indices, the questions addressed a variety of topics such as the time business owners spend on administrative tasks; the type of licenses they have and how easy or complex they think the procedures are to obtain them; how much various business procedures cost in terms of time and money; their comprehension of regulations and access to business documentation; the dynamism of provincial leadership; informal charges and protection payments; whether businesses have commercial disputes and their resolutions; whether they have regular exchanges with public officials; as well as battery of questions about their business performance and plans.

In addition to the 1082 firms of stage 2, and using the same questionnaire, **152 firms/establishments** already covered by the PBES 2006 were re-interviewed. This panel group is critical for measuring the evolution of business environments, as perceived by individual firms

between 2006 and 2009 in the 10 provinces covered by the first PBES. This panel group was composed of businesses randomly sampled from within the firms already surveyed in the 2006 PBES. The panel is especially useful, because their aggregate perceptions are impervious to sampling error. They experienced the business environment in 2006 and can directly compare their own recollections with current conditions.

Table 36 provides descriptive information on the respondents who answered the survey. Four samples of businesses are compared. Column 1 assesses the entire PBES sample of 1,234 operations in 2009 without re-weighting. These data provide an accurate reflection for each province, but cannot be used for national-level analysis. By stratifying at the provincial level, the PBES data tends to under-estimate large provinces such as Phnom Penh and Battambang. To provide national-level conclusions based on the PBES survey, Table 36 reweights answers by the proportion of Cambodia's total firms in each province, so that Phnom Penh's importance to the economy is accurately reflected in the data. These proportions are the same ones shown in Figure 2 above. Descriptive statistics by the national-level weighting can be viewed in Column 4. For comparative purposes, descriptive data is also provided just for firms in the ten provinces originally surveyed in 2006 (Column 2) and for the 152 panel respondents (Column 3).

Table 36: Who Answered the 2009 PBES Survey?
(Composition of the 1234 Total Respondents)

| | Provincially Representative Sample ¹ | Original 10 Provinces ² | Panel Respondents ³ | Nationally Representative Sample ⁴ |
|---|--|------------------------------------|--------------------------------|--|
| Observations | 1234 | 675 | 152 | 1234 |
| Respondent's Position in Firm | | | | |
| Owner and Primary Manager | 88.2% | 86.4% | 92.8% | 83.2% |
| Owner without Management Responsibilities | 1.30% | 0.74% | 1.3% | 2.5% |
| General Manager | 6.16% | 7.70% | 2.6% | 10.2% |
| Employee | 1.30% | 2.37% | 3.3% | 2.53% |
| Relative of Owner | 4.16% | 2.82% | | 1.6% |
| Establishment Year | | | | |
| Before 1991 | 6.2% | 7.9% | 7.9% | 8.2% |
| Between 1991 and 1996 | 13.7% | 15.6% | 23.7% | 15.6% |
| Between 1997 and 2002 | 23.6% | 23.6% | 30.3% | 18.0% |
| After 2002 | 56.5% | 53.0% | 38.2% | 58.1% |
| Size of Firm (Number of Employees) | | | | |
| 2 or less | 62.2% | 58.1% | 54.6% | 52.3% |
| Between 3 and 5 | 24.1% | 25.3% | 27.0% | 26.1% |
| Between 6 and 10 | 8.8% | 9.8% | 12.5% | 12.7% |
| Between 11 and 30 | 4.4% | 5.9% | 5.9% | 7.7% |
| More than 30 | 0.6% | 0.9% | 0.0% | 1.3% |
| Percent Seasonal Hires | 4.5% | 4.9% | 5.2% | 3.8% |
| Primary Sector of Operations | | | | |
| Manufacturing | 9.1% | 8.6% | 7.9% | 9.0% |
| Construction | 0.2% | 0.4% | 0.0% | 0.1% |
| Service/Commerce | 90.4% | 90.5% | 90.8% | 90.7% |
| Agriculture/Aquaculture | 0.2% | 0.4% | 1.3% | 0.1% |
| Primary Sales Location | | | | |
| In Home Province of Firm | 89.4% | 90.5% | 98.0% | 86.1% |
| In Other Cambodian Provinces | 0.7% | 1.0% | 1.3% | 0.9% |
| Exported Internationally | 9.9% | 8.4% | 0.7% | 13.1% |
| Plans over Next Two Years | | | | |
| Increase Size of Operations Considerably | 18.9% | 19.3% | 19.1% | 17.1% |
| Increase Size of Operations | 41.1% | 38.2% | 32.9% | 32.8% |
| Continue Operating at Present Size | 36.2% | 38.2% | 41.5% | 45.5% |
| Reduce Size of Operations | 1.9% | 2.1% | 3.3% | 1.1% |
| Reduce Size of Operations Considerably | 0.5% | 0.4% | 0.7% | 0.6% |
| Plan to Close this Business | 1.4% | 1.8% | 2.6% | 2.9% |

¹. PBES Sample employing stratified random sample to mirror population in all 24 provinces;
². Analysis limited to ten provinces studied in 2006;
³. Includes only 152 surveyed in both 2006 and 2009;
⁴. Re-weighted PBES sample to reflect the national proportion of firms within each province.

8.1.3 Open-Ended Interviews

In addition to the standard questionnaire used for the survey, 85 firms/establishments were interviewed to develop case-studies and collect quotes that are included as vignettes in this and other publications.

8.2 Constructing the PBES

Figure 22 below presents flow-chart of the PBES creation process. In sum, we begin with the collection of indicators from survey and hard data, standardize them to a 10-point scale, compile them into theoretically motivated sub-index, and finally add them into the final Cambodian PBES.

8.2.1 Choosing the Sub-indices and Constructing the Score

Once survey data is collected, responses of business owners are aggregated at the provincial level. Province-level indicators are selected to capture critical areas of economic governance for private sector development.

Dealing with Perception Bias

As 90% of businesses only do business inside their home province, there is a strong probability of perception bias. It is difficult for business owners to rank their provincial leaders fairly against other leaders when they have no idea what the business environment is like in other jurisdictions. We address this dilemma in two ways. First, the survey questions selected for inclusion in the index are heavily tilted towards more concrete (often countable) concepts, such as “How many regulatory inspections did your firm experience in the past month?” as opposed to more abstract approaches like, “Rank the burden of inspections on a five-point scale.” In some cases, however, abstract questions are necessary to truly capture the

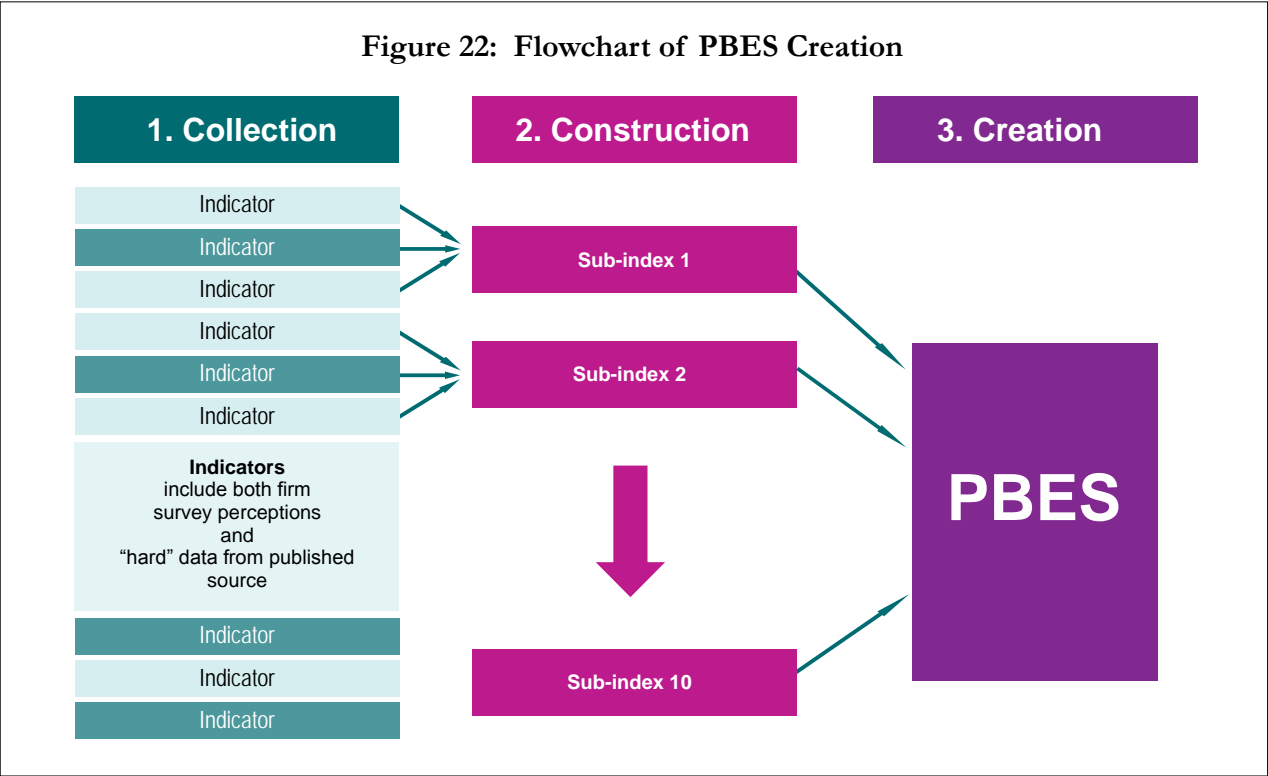
business environment concept under study. Recognizing that perception bias can affect rankings in these cases, we merge secondary data into these sub-indices to correct for the bias. For instance, in the transparency sub-index we did not rely solely on firm perceptions of access to business information; instead, we sent a team of researchers to provincial agencies in each province to record whether they could easily obtain basic documentation necessary to register and run a business in the locality. Two forms of secondary data are employed. Data from published and verifiable sources and data from self-observation, derived from sending a research team to every province to record basic facts about regulatory procedures.

Standardizing Indicators

Appendix 1 below provides a full listing of all sub-indices and indicators included within them. Descriptive information for each indicator is also provided, allowing over-time comparisons. Each indicator within a sub-index is standardized to a 10-point scale, with 10 representing the best score recorded in Cambodian that year and 1 the worst. All other provinces rank somewhere between these two end points.

Constructing Sub-indices

Construction of sub-indices is based both on broad concepts discussed internationally among economists, and more narrow categories of Cambodian-specific business obstacles. Using these theoretical guides, particular indicators are selected to represent the concept covered by each sub-index. Sub-indices are calculated by taking the simple average of their composite indicators. As a result, they are also on a 10-point scale. When secondary data is included in a sub-index, a weighted average is employed to ensure that secondary data accounts for 40% of the sub-index score. This is enough to correct for perception bias, but not enough to dominate the opinions of respondents.



Assembling the Final PBES

After the creation of sub-indices, a final PBES score can be efficiently assembled by summing up the sub-indices. Different weighting approaches are certainly possible. In 2006, the number of provinces was too small to objectively create weights by determining the impact of individual sub-indices on key outcome variables of interest to policy-makers (number of firms, investment growth, and profitability) using regression analysis. With more data this year, such an operation is possible. Nevertheless, we maintain the same non-weighted approach to facilitate over-time comparisons. Table 3 on page 17 above, however, does provide the analysis of the most important sub-indices. Interested users can supply their own weightings, as they see fit.

8.2.3 Advantages of a Relative Approach

Three features of the PBES approach are worth noting. First, the scores are generated by comparing an individual province to the best and worst provinces on a particular indicator. By normalizing the scores around best economic governance practices already found in Cambodia and not against ideal and possibly unattainable standards of good governance, the PBES encourages sub-national governments to improve their performance. For each indicator, a “star” or top-performing locality can be identified and any other province can conceivably attain a perfect score of 100 in future iterations by emulating these Cambodian best practices.

Second, the PBES is solely a measure of economic governance and regulatory policy. It does not assess initial conditions for development (that is, the fundamental underlying factors that contribute to economic growth in a province but that are virtually impossible to address in the short term, such as location, infrastructure, size of the domestic market, and human resources). In doing so, the PBES is able to rank all provinces on an equal basis without giving undue advantage to well-endowed locations. Thus, the PBES should not be confused with a measure of 'Total Investment Environment' that includes both governance and measures of initial endowments (i.e. structural conditions).

Third, the indicators that comprise the PBES are actionable in the sense that they are specific items that provincial officials can target and monitor improvement upon, and they are action-worthy because they represent policies that private firms have identified as critical to their business success and that previous research has shown to be influential for firm performance.

The same 10 sub-indices used in 2006 PBES are used to allow for over-years comparison. They were designed to highlight private sector priorities as well as focus on the issues that can be influenced by provincial government.

8.3 Relationship Between the 2006 and 2009 PBES Results

For a comparative ranking such as the PBES, it is important to demonstrate that rankings do not change substantially from year to year. This consistency has important policy

and methodological implications. In terms of policy, the stability of the rankings indicates that provincial reforms have long-lasting effects. They do not dissipate at the end of the calendar year; firms continue to benefit from them and recall their impact when questioned by interviewers.

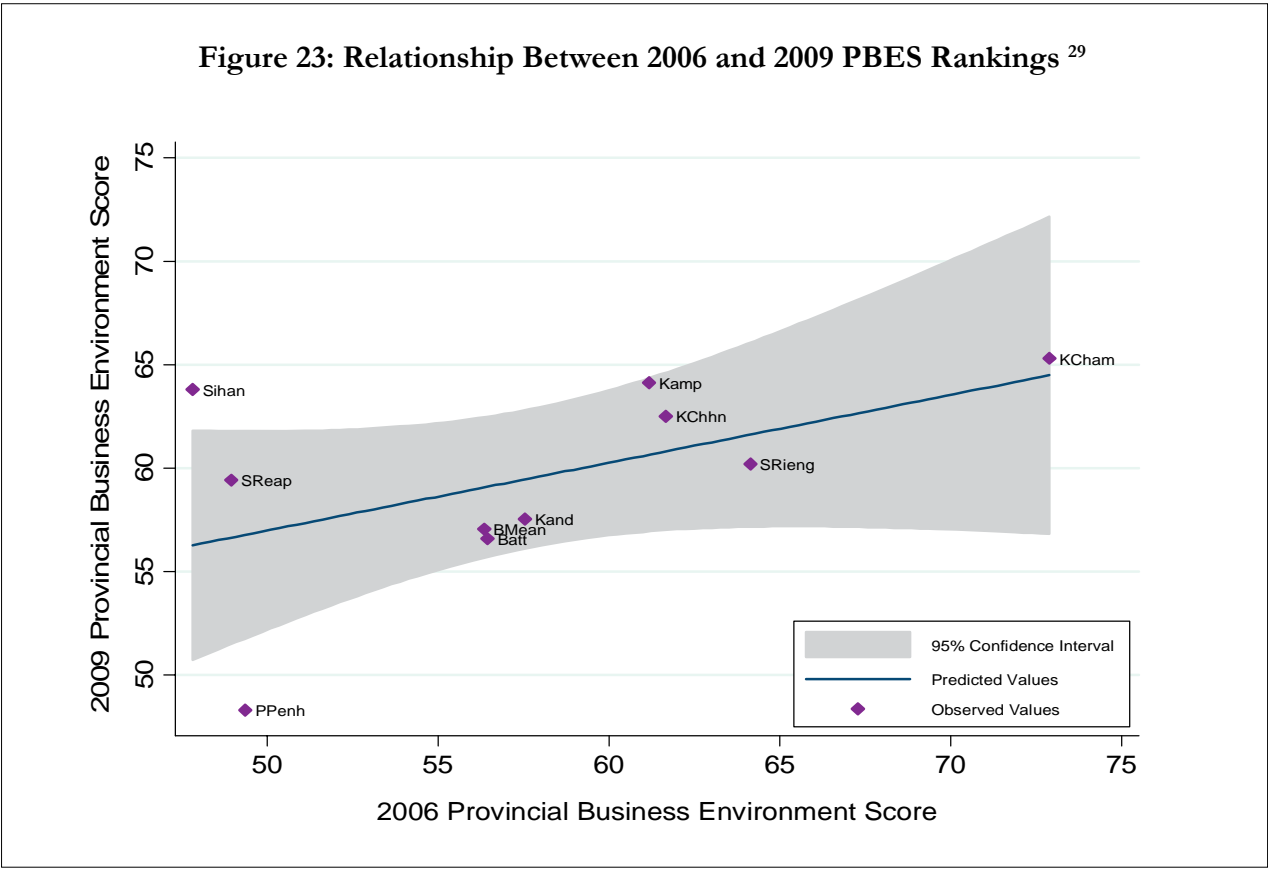
Methodologically, the strong correlation with PBES rankings in 2006 indicates that ranking provinces against each other works quite well. The PBES can consistently identify top performers, while also identifying what lower ranking provinces need to do to improve their scores in future. Such stability is confirmation that the approach offers a consistent and accurate measure of provincial economic governance over time.

Figure 23 is a scatter-plot illustrating the relationship between the 2006 and 2009 PBES scores and rankings for the same 10 provinces. The first thing to notice about this figure is that it is very likely that past performance is an important determinant of future governance. The graph shows that past performance is an important determinant of future governance.²⁸ The line shows, based on the 2006 PBES scores, what one would expect the province's 2009 PBES score to be.

It is important to note that 'stability' in the scores does not mean that the scores cannot change. Over the past two years, a number of provinces climbed up the PBES ladder. These provinces can be identified immediately in Figure 23, as their actual 2009 PBES scores are above the prediction line.

²⁸ The correlation coefficient, as a measure of the standardized covariance between 2006 and 2009 PBES, is 0.49 and is significant at the .05 level.

Figure 23: Relationship Between 2006 and 2009 PBES Rankings ²⁹



²⁹ The shaded region shows a 95% confidence interval around that line. A confidence interval means that were we to repeat the PBES exercise and re-sample a new set of firms, 95% of the time, the true correlation line between the 2006 and the 2009 scores would lie within that region. The relationship may not be exactly the same, but we can say for certain that past performance would continue to be a strong and positive determinant of future governance.

Appendix 1: Detailed Descriptions of Sub-indices and Component Indicators

1. Entry Costs

- % of firms registered with the Ministry of Commerce or Municipal Department of Commerce
- Total number of registrations, licenses and permits firms need to operate
- Waiting period for Registration Certificate from Provincial/Municipal Department of Commerce (median days)
- Official fee for Registration Certificate from Provincial/Municipal Department of Commerce (median \$)
- Waiting period for One-Year Operating License (median days)
- Official fee for One-Year Operating License (median \$)
- Waiting period for Patent Tax registration from Local Tax Authority (median days)
- Official Patent Tax Fee from Local Tax Authority (median \$)
- Provincial Revenue from Patent Tax *
- Provincial Revenue from Registration certificate *

2. Property Rights

- % of firms with land documentation
- % of firms with solid title to land
- % of firms that feel expropriation is a risk
- % of firms that deem changes in rental contracts a risk
- Effective land prices (adjusted for differences in supply and demand) (mean \$)**

3. Transparency

- Transparency of - and access to - local planning and decrees/decisions (10 documents/5-point scale)
- Firm's knowledge of provincial budget (% not familiar)
- Relationship with a provincial official is necessary to obtain access to provincial documents (% always or frequently)
- % of firms agreeing that favoritism toward firms with political connections is an obstacle to business.
- Regularity that representatives from the provincial governor's office meet with firms to discuss changes in laws or policies (% seldom or Never)
- Firms are informed about new economic and finance regulations that affect their business (% uniformed or poorly informed)
- Regularity that a firm receives advance notice about new or changing central government laws (% Seldom or Never)
- Request to Provincial/Municipal Department of Commerce * (5-point scale)
- Request to Provincial/Municipal Departments of Industry, Mines and Energy * (5-point scale)
- Availability of infrastructure maps * (# offices with map available)

4. Time Costs of Regulatory Compliance

- Management time during year spent dealing with requirements imposed by government regulations (% of firms less than 16 days)
- Total number of inspections per year (median)
- Time it took a firm to receive its land title (median days)

5. Informal Charges

- Giving gifts to public officials is sometimes required to pass customs, obtain licenses, receive public services, or meet tax requirements (% No)
- Corruption is an obstacle (% of major or severe obstacle)
- Information regarding available public procurement contracts is transparent (% Always or Frequently)
- Importance of government connections for winning public procurement contracts (% Essential or Useful)
- Firms believe firms in their industry often pay commissions when doing business with government (% of Seldom or Never)

- Other agencies ask for additional payment (%Yes)
- Firms usually know how much additional payment is required in their industry (% agree)
- Regularity that services are delivered as expected when a firm pays the required additional payment (% regularly or always)
- Bribes are useful for business (% Agree)

6. Participation

- % of firms agreeing provincial government solicits advice from affected firms on new laws, rules, regulations or decrees
- There are business associations or clubs in the province (% Yes)
- % of firms in sample that are members of associations or clubs in the province
- Number of business associations per 10,000 firms in province *
- Business Forum held in 2007 *
- Evidence of visible suggestion boxes in DIME or DOC or other mode of aggregating business complaints to Commune Council in DIME or DOC * (No evidence to three different channels)

7. Crime Prevention

- % of firms that experienced losses due to theft, robbery, vandalism, or arson in last year (% No)
- Monetary value of firm's losses caused by crime (median \$)
- % of firms that believe firms in their sector make protection payments to the police
- % of firms that pay protection money to others

8. Tax Administration and Burden

- % of firms that believe bribes to public officials to avoid taxes and regulations are a significant business obstacle
- % of firms that do not pay taxes
- % of firms that believe negotiating with tax authority is part of business
- Tax administration is an obstacle (%)
- Tax rates as obstacle (%)

9 Proactivity of Provincial Authorities

- Provincial government officials' attitude toward private business (% positive)
- Provincial departments of line ministries tend to interpret in firms' favor when central regulation lacks clarity (% agree)
- Provincial government is good at working within central laws to create a profitable business environment (% agree)
- Provincial government is creative and clever about solving new business problems (% agree)
- Provincial government willingly risks punishment from the central government to pass decisions to aid local businesses (% agree)
- There are no initiatives at the provincial level (%)

10 Dispute Resolution

- % of firms that are confident that the legal system will uphold contracts and property rights in disputes
- Possibility of going to another official to dispute unjust decision (% seldom or never)
- Percentage of sales in 2008 for which firm did not receive payment in the agreed time (median)
- Percentage of sales for which firm never paid by customers in 2008 (median)
- Satisfaction with dispute resolution in province (% satisfied)
- Success at recovering money owed to it (% successful)
- % of firms in province that believe there is a fair process to dispute changes in rent contracts

* component uses hard data; ** Derived from factor analysis; all other indicators derived from perception data

Appendix 2: Changes over Time on Indicators Used in Sub-indices

| Comparison of Entry Costs Sub-index (2006-2009) | | | | |
|--|---------|------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| Business registered with the Ministry of Commerce or Municipal Commerce Division (%). | Min | 25 | 1.9 | 1.9 |
| | Median | 45 | 23.7 | 27.8 |
| | Max | 67.5 | 65 | 57.7 |
| Total registrations, licenses (environmental, labor, wood processing, construction, etc.), and permits does your firm presently need to operate (please count all the licenses, permits, stamps, etc. issued by different agencies, even if they deal with the same type of activity)? (% > 5 documents) | Min | 0 | 0 | 1.8 |
| | Median | 5 | 3.8 | 3.8 |
| | Max | 13.5 | 11.5 | 11.5 |
| Waiting period for Registration Certificate for Provincial Department of Commerce (Median Days) | Min | 10 | 2 | 8.00 |
| | Median | 20 | 15 | 16.75 |
| | Max | 30 | 90 | 30 |
| Waiting period for One Year Operating License (Median Days) | Min | 7 | 2 | 7 |
| | Median | 15 | 14 | 21.25 |
| | Max | 30 | 30 | 30 |
| Waiting period Patente Tax from Local Tax Authority (Median Days) | Min | 8.5 | 2.5 | 7 |
| | Median | 15 | 7 | 12.5 |
| | Max | 30 | 30 | 30 |
| Official fee for Registration Certificate from Provincial Department of Commerce (Median \$) | Min | 3.75 | 5 | 5 |
| | Median | 12.5 | 15 | 16.25 |
| | Max | 30 | 50 | 42.5 |
| Official fee for Operating License (Median \$) | Min | 2.25 | 6.5 | 6.5 |
| | Median | 12.5 | 15 | 16 |
| | Max | 35 | 50 | 40 |
| Official fee for Patente Tax (Median \$) | Min | 8.5 | 7.5 | 5 |
| | Median | 15 | 14 | 10 |
| | Max | 30 | 25 | 25 |
| Provincial Revenue from Registration Certificate (\$) | Min | 0.5 | 1.4 | 1.3 |
| | Median | 5.8 | 1.8 | 17.9 |
| | Max | 33.3 | 34.7 | 34.7 |
| Provincial Revenue from Patent Tax (\$) | Min | 1.2 | 0.2 | 1.4 |
| | Median | 4.1 | 2.2 | 4.4 |
| | Max | 12.3 | 11.9 | 11.9 |

All scores are provincial aggregates

| Comparison of Property Rights Sub-index (2006-2008) | | | | |
|---|---------|-------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| Firms with formal land title (including solid title, pre-2000 title, and soft title, %). | Min | 69.6 | 57.9 | 79.5 |
| | Median | 87.3 | 93.5 | 96.2 |
| | Max | 95.8 | 100.0 | 100.0 |
| Firms with solid title or pre-2000 title (%) | Min | 47.1 | 18.5 | 35.9 |
| | Median | 58.5 | 57.7 | 68.9 |
| | Max | 85.4 | 95.5 | 95.5 |
| Risk of Expropriation (% Always or Frequently) | Min | 0.0 | 0.0 | 0.0 |
| | Median | 4.5 | 3.9 | 3.0 |
| | Max | 14.0 | 33.3 | 9.0 |
| Risk of Change in Rental Contract (% Always or Frequently) | Min | 10.4 | 0 | 5.6 |
| | Median | 19.2 | 16.6 | 20.9 |
| | Max | 40.0 | 40.7 | 40.7 |
| Effective Price of Land (\$/M Squared, Residual from Regression Analysis Controlling for Demand, Supply, and Structural Conditions) | Min | -82.6 | -361.7 | -361.7 |
| | Median | -56.6 | 0 | -61.3 |
| | Max | 215.5 | 322.13 | 322.13 |

All scores are provincial aggregates
 NA: Indicators not used in 2006.

| Comparison of Transparency Sub-index (2006-2009) | | | | |
|---|---------|-------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| Access to Provincial Regulatory Information (Factor Analysis of 11 Provincial Documents) | Min | -0.34 | -0.94 | -0.94 |
| | Median | -0.07 | -0.03 | 0.00 |
| | Max | 0.59 | 0.95 | 0.43 |
| Firms without knowledge of the provincial budget (%) | Min | 4.6 | 5.7 | 5.7 |
| | Median | 57.5 | 23.3 | 20.1 |
| | Max | 80.0 | 54.7 | 54.7 |
| Relationship necessary to access provincial documents (% Always or Often) | Min | 7.5 | 40.0 | 47.1 |
| | Median | 15.2 | 54.9 | 54.9 |
| | Max | 29.2 | 84.6 | 84.6 |
| Favoritism toward politically connected firms (%) | Min | 35.4 | 15 | 17.3 |
| | Median | 52.5 | 38.9 | 47.1 |
| | Max | 67.5 | 67.3 | 67.3 |
| How often do representatives from the provincial governor's office or provincial meet with you and other private domestic businesses to discuss changes in laws or policies (% Seldom or Never) | Min | 67.7 | 65 | 65.4 |
| | Median | 85.3 | 80.4 | 80.8 |
| | Max | 97.5 | 94.3 | 94.3 |
| How informed are you about new rules, laws, and regulations about economics and finance which materially affect your business (% Poorly or Uninformed) | Min | 67.7 | 53.5 | 53.5 |
| | Median | 82.22 | 71.8 | 73.1 |
| | Max | 92.5 | 95 | 81.6 |
| How often do you receive advance notice about changes in central government laws (% Seldom or Never) | Min | 67.5 | 35 | 40.4 |
| | Median | 82.22 | 71.8 | 63.8 |
| | Max | 95 | 85 | 78.2 |
| Request to Provincial Department of Commerce (1 (Low) to 5 (High)) | Min | 1 | 1 | 1 |
| | Median | 2 | 2 | 2 |
| | Max | 4 | 4 | 5 |
| Request to Provincial Department of Industry Mines and Energy (1 (Low) to 5 (High)) | Min | 1 | 1 | 1 |
| | Median | 2 | 2 | 2 |
| | Max | 4 | 3 | 3 |
| Infrastructure Maps Available (# Offices with Map Available) | Min | | 0 | 0 |
| | Median | NA | 1 | 0.5 |
| | Max | | 2 | 2 |

All scores are provincial aggregates
 NA: Indicators not used in 2006.

| Comparison of Participation Sub-index (2006-2009) | | | | |
|---|---------|------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| When a new law, rule, regulation or decree is being discussed that could have a substantial impact on your business, does the provincial government solicit advice from firms like yours regarding the content or implementation of the legal document? (% Always or Regularly) | Min | 0.0 | 1.0 | 1.0 |
| | Median | 2.5 | 3.3 | 3.8 |
| | Max | 7.5 | 10.0 | 10.0 |
| Business Association in Province (% Agree) | Min | 2.5 | 0.0 | 3.8 |
| | Median | 10.1 | 7.5 | 10.1 |
| | Max | 40.0 | 19.6 | 19.6 |
| Firm is a member of Business Association (%) | Min | 0.0 | 0.0 | 0.0 |
| | Median | 1.3 | 0.0 | 1.9 |
| | Max | 5.0 | 5.8 | 5.8 |
| Business Associations per 10,000 Firms in Province | Min | 0.0 | 0 | 0 |
| | Median | 10.9 | 3.8 | 5.55 |
| | Max | 38.6 | 55.6 | 26.6 |
| Business Forums held in 2008 | Min | | 0 | 0 |
| | Median | NA | 2 | 2.5 |
| | Max | | 21 | 21 |
| Visible suggestion boxes in DIME or DOC | Min | | 0 | 0 |
| | Median | NA | 0 | 0 |
| | Max | | 1 | 1 |
| Mode of aggregating business complaints to Commune Councils in DIME or DOC | Min | | 0 | 0 |
| | Median | NA | 1 | 1 |
| | Max | | 2 | 2 |

All scores are provincial aggregates
NA: Indicators not used in 2006.

| Comparison of Time Costs of Regulatory Compliance Sub-Index (2006-2009) | | | | |
|---|---------|------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| In a typical week in 2005, what percentage of the total time of owners or high-level managers was spent in dealing with requirements imposed by government regulations [e.g. taxes, customs, labor regulations, licensing and registration] including dealings with officials, completing forms, etc? (% >=16 Days) | Min | 0.0 | 0.0 | 0.0 |
| | Median | 14.6 | 18.5 | 26.7 |
| | Max | 28.8 | 43.2 | 40.5 |
| Median business inspections in 2008 | Min | 3 | 0 | 0.5 |
| | Median | 4 | 2 | 2 |
| | Max | 12 | 12 | 4 |
| Wait for land (median days) | Min | 30 | 7 | 15 |
| | Median | 58 | 30 | 30 |
| | Max | 75 | 165 | 165 |

All scores are provincial aggregates

| Comparison of Informal Charges Sub-index (2006-2009) | | | | |
|---|---------|-------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| Gifts or informal charges a normal part of doing business (% No) | Min | 32.50 | 42.5 | 44.9 |
| | Median | 56.25 | 65.8 | 52.80 |
| | Max | 67.69 | 97.5 | 82.70 |
| Corruption is an obstacle (% Major or Severe) | Min | 25.6 | 10.0 | 14.9 |
| | Median | 33.8 | 37.0 | 41.8 |
| | Max | 63.1 | 55.8 | 55.8 |
| Bribes are useful for business (% Agree or S. Agree) | Min | | 10.0 | 15.4 |
| | Median | NA | 30.0 | 31.3 |
| | Max | | 45.0 | 42.3 |
| Believe that information regarding available public procurement contracts is transparent? (% Always or Frequently) | Min | 2.5 | 0 | 1.9 |
| | Median | 17.5 | 18.8 | 18.8 |
| | Max | 26.2 | 30.6 | 30.6 |
| Personal connections to government officials necessary for winning public procurement contracts (% Essential or Useful) | Min | 45.0 | 39.6 | 39.6 |
| | Median | 67.5 | 60.8 | 62.3 |
| | Max | 85.0 | 75 | 75 |
| Pay commission when doing business with government (% Never or Seldom) | Min | 8.7 | 0 | 8.9 |
| | Median | 39.7 | 31.4 | 25.1 |
| | Max | 58.3 | 66.7 | 55.8 |
| Know size of informal payment (% Yes) | Min | 12.5 | 7.5 | 19.2 |
| | Median | 25.3 | 20.9 | 28.2 |
| | Max | 48.9 | 46.1 | 46.1 |
| Other agencies ask for additional payments (% Yes) | Min | 7.5 | 5 | 7.5 |
| | Median | 17.2 | 24 | 31.5 |
| | Max | 42.5 | 42.5 | 42.3 |
| After bribe, service is delivered (% Frequently or Always) | Min | 10.00 | 2.5 | 13.5 |
| | Median | 21.12 | 27.5 | 29.1 |
| | Max | 36.92 | 57.7 | 57.7 |

All scores are provincial aggregates
 NA: Indicators not used in 2006.

| Comparison of Crime Prevention Sub-index (2006-2009) | | | | |
|--|---------|------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| Establishment experience losses in the last year due to theft, robbery, vandalism, or arson (% No) | Min | 45.0 | 60.0 | 60.0 |
| | Median | 70.0 | 86.1 | 78.1 |
| | Max | 92.5 | 97.2 | 91.7 |
| Estimated value of losses due to crime (Median \$) | Min | 48 | 30 | 30 |
| | Median | 60 | 125 | 100 |
| | Max | 125 | 1025 | 200 |
| Firms make protection payments to police (% Yes) | Min | 2.5 | 0.0 | 0.0 |
| | Median | 11.2 | 5.1 | 9.5 |
| | Max | 27.8 | 30.4 | 30.4 |
| Firms make protection payments to others (% Yes) | Min | 0.0 | 0.0 | 0.0 |
| | Median | 9.6 | 0.0 | 1.5 |
| | Max | 18.9 | 4.7 | 4.7 |

All scores are provincial aggregates

| Comparison of Proactivity Sub-index (2006-2009) | | | | |
|--|---------|------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| Attitude of provincial government officials toward private business? (% Positive) | Min | 24.6 | 13.5 | 13.5 |
| | Median | 36.3 | 41.8 | 34.7 |
| | Max | 52.5 | 57.7 | 57.7 |
| If there is a lack of clarity on certain regulations at national level, the provincial governments tends to interpret in my favor (%). | Min | 7.5 | 5.8 | 5.8 |
| | Median | 17.2 | 12.8 | 13.4 |
| | Max | 37.5 | 47.5 | 46.2 |
| Provincial government is very good at working within laws to create a profitable private business environment (%) | Min | 49.2 | 48.6 | 48.6 |
| | Median | 57.5 | 62.0 | 58.4 |
| | Max | 82.5 | 77.5 | 73.1 |
| Provincial government is creative and clever about solving new business problems (%) | Min | 33.9 | 35.0 | 39.6 |
| | Median | 54.4 | 53.9 | 52.4 |
| | Max | 77.5 | 72.5 | 67.3 |
| Provincial government is willing to risk punishment from the central government to pass decisions that may aid my business (%) | Min | 12.5 | 20.0 | 20.0 |
| | Median | 25.0 | 30.8 | 30.8 |
| | Max | 47.5 | 51.3 | 50.0 |
| No initiatives at the provincial level, all policies come from the central government (%) | Min | 15.4 | 10.0 | 17.0 |
| | Median | 29.9 | 32.5 | 30.2 |
| | Max | 40.0 | 57.7 | 57.7 |

All scores are provincial aggregates

| Comparison of Tax Administration Sub-index (2006-2009) | | | | |
|--|---------|------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| Firms not paying any taxes at all (%) | Min | 5.0 | 15.0 | 23.1 |
| | Median | 21.3 | 30.9 | 38.1 |
| | Max | 47.8 | 71.8 | 55.2 |
| Bribe to public officials to avoid taxes and regulations are an obstacle to business (%) | Min | 50.0 | 52.9 | 59.0 |
| | Median | 80.5 | 75.8 | 75.7 |
| | Max | 97.2 | 90.9 | 89.7 |
| Negotiations with tax authority are a necessary part of doing business (%) | Min | 44.0 | 25.0 | 25.0 |
| | Median | 63.9 | 57.9 | 53.8 |
| | Max | 72.4 | 87.1 | 78.8 |
| Tax rates are an obstacle to business (%) | Min | 2.5 | 0.0 | 1.9 |
| | Median | 12.5 | 8.8 | 13.8 |
| | Max | 21.5 | 40.0 | 24.6 |
| Tax administration is an obstacle to business (%) | Min | 0.0 | 2.5 | 5.8 |
| | Median | 2.5 | 16.3 | 15.4 |
| | Max | 15.4 | 35.0 | 31.8 |

All scores are provincial aggregates

| Comparison of Dispute Resolution Sub-index (2006-2009) | | | | |
|---|---------|------|-----------|------------------|
| Indicator | Measure | 2006 | 2009 Full | 2009 Original 10 |
| Percentage of sales that were repaid late (Median) | Min | 0.0 | 0.0 | 0.0 |
| | Median | 4.3 | 4.0 | 4.5 |
| | Max | 10.0 | 20.0 | 10.0 |
| Percentage of sales that were never repaid (Median) | Min | 2.0 | 0.0 | 1.0 |
| | Median | 3.0 | 3.0 | 2.8 |
| | Max | 10.0 | 5.0 | 5.0 |
| Confident that legal system will uphold property rights (%) | Min | 6.5 | 1.9 | 1.2 |
| | Median | 33.8 | 26.5 | 21.9 |
| | Max | 57.5 | 57.5 | 42.3 |
| If government agency acts against the rule (overzealous inspectors, unofficial payments), issue can be challenged (%) | Min | 40.0 | 20.0 | 36.5 |
| | Median | 64.0 | 69.1 | 67.8 |
| | Max | 87.5 | 95.0 | 90.4 |
| Firm was satisfied with resolution of final dispute (%). | Min | 28.1 | 18.8 | 28.6 |
| | Median | 46.6 | 37.5 | 41.0 |
| | Max | 55.6 | 71.4 | 71.4 |
| Successful at recovering money owed firms (%) | Min | 26.3 | 28.6 | 18.8 |
| | Median | 46.6 | 41.0 | 35.1 |
| | Max | 61.5 | 71.4 | 59.1 |

All scores are provincial aggregates

Appendix 3: Association between PBES and Willingness to Expand or Shrink Business Activity

| Independent Variables | Full-Scale | | | | | | Expand Dichotomous | | Decline | Close |
|---------------------------------|--------------------|--------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|----------------------|----------------------|
| | (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) | (9) | (10) |
| Total PBES | 0.015** (0.007) | 0.015 (0.010) | 0.017 (0.011) | 0.017** (0.008) | 0.017** (0.007) | 0.017** (0.008) | 0.010*** (0.003) | 0.027*** (0.006) | -0.028*** (0.010) | -0.065*** (0.014) |
| Business Nationally Registered | | 0.238** (0.108) | 0.186 (0.117) | 0.181 (0.128) | 0.174 (0.129) | 0.197 (0.140) | 0.066 (0.059) | 0.155 (0.152) | 0.016 (0.220) | 0.068 (0.448) |
| Business Provincial Registered | | -0.013 (0.097) | -0.059 (0.097) | -0.025 (0.110) | -0.021 (0.112) | -0.019 (0.112) | -0.035 (0.043) | -0.089 (0.110) | 0.255 (0.164) | 0.340 (0.251) |
| Total Firm Assets in 2008 | | | 0.000 (0.000) | 0.000 (0.000) | 0.000 (0.000) | 0.000 (0.000) | 0.000* (0.000) | 0.000 (0.000) | -0.000 (0.000) | 0.000 (0.000) |
| Labor Size | | | 0.107*** (0.037) | 0.105*** (0.038) | 0.105*** (0.038) | 0.099*** (0.039) | 0.018 (0.020) | 0.049 (0.051) | -0.116 (0.095) | -0.230 (0.169) |
| Growth in Sales (2006 to 2008) | | | | | 0.000 (0.000) | 0.000 (0.000) | 0.000 (0.000) | 0.000 (0.000) | 0.000 (0.000) | -0.004 (0.004) |
| Exporting Firm | | | | -0.003 (0.004) | -0.004 (0.005) | -0.003 (0.005) | -0.001 (0.004) | -0.004 (0.009) | | |
| Percentage of Roads (Asphalted) | | | | -0.003 (0.003) | -0.003 (0.003) | -0.003 (0.003) | -0.001 (0.001) | -0.002 (0.004) | 0.002 (0.004) | -0.002 (0.010) |
| Distance from Ports (km) | | | | 0.000 (0.000) | 0.000 (0.000) | 0.000 (0.000) | 0.000 (0.000) | 0.001 (0.000) | 0.000 (0.001) | -0.000 (0.001) |
| Provincial Literacy Rate (%) | | | | -0.002 (0.002) | -0.002 (0.002) | -0.001 (0.002) | -0.000 (0.001) | | | |
| Sector Fixed Effects | NO | NO | NO | NO | NO | YES | YES | NO | NO | NO |
| Observations | 1234 | 1234 | 1234 | 1115 | 1106 | 1106 | 1106 | 1106 | 1234 | 1234 |
| Pseudo R-Squared | 0.00163 | 0.00377 | 0.00789 | 0.0136 | 0.0139 | 0.0158 | 0.0260 | 0.0245 | 0.0207 | 0.0858 |
| Chi2 | 4.862 | 8.564 | 39.18 | 34.17 | 34.28 | | | 74.76 | 31.87 | 39.45 |
| Log Likelihood | -1490 | -1487 | -1481 | -1334 | -1322 | | | -726 | -171.7 | -68.6 |

Probit Model of Business Expansion. Marginal Probabilities with Robust Standard errors , clustered at provincial level, in parentheses; *** p<0.01, ** p<0.05, * p<0.1; Dependent Variable is the full likert scale ranging from (1) Close Business to (6) Expand Considerably for Models 1-6. For models 7 and 8, we use a dichotomous measure for whether firm expanded business (values 5 & 6 in original question). Model 9 is a dichotomous measure of business decline (values 1 & 2 in original question). Model 10 is a dichotmous measure of business closure (value 1 in original question).

Appendix 4: Association between Sub-indices and Willingness to Expand Business

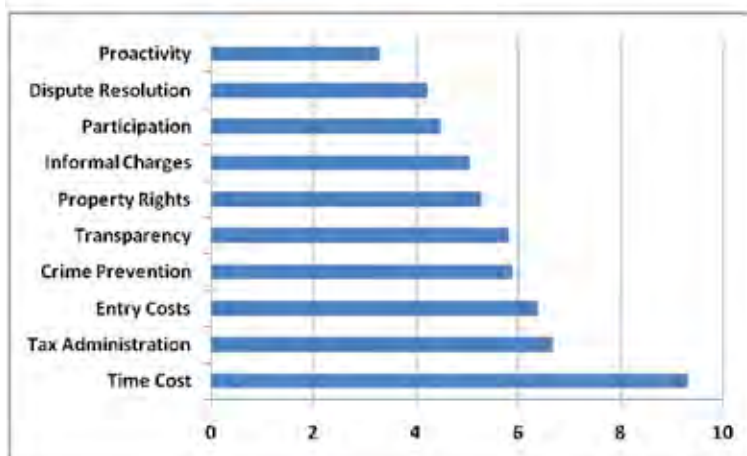
| Independent Variables | (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) | (9) | (10) |
|---------------------------------|----------|---------|---------|----------|---------|---------|---------|----------|---------|---------|
| Subindex 1: Entry | 0.033*** | | | | | | | | | |
| | -0.011 | | | | | | | | | |
| Subindex 2: Property | | 0.002 | | | | | | | | |
| | | -0.014 | | | | | | | | |
| Subindex 3: Transparency | | | -0.01 | | | | | | | |
| | | | -0.022 | | | | | | | |
| Subindex 4: Time | | | | 0.033*** | | | | | | |
| | | | | -0.013 | | | | | | |
| Subindex 5: Informal Charges | | | | | 0.035* | | | | | |
| | | | | | -0.018 | | | | | |
| Subindex 6: Participation | | | | | | 0 | | | | |
| | | | | | | -0.012 | | | | |
| Subindex 7: Crime Prevention | | | | | | | 0.027** | | | |
| | | | | | | | -0.012 | | | |
| Subindex 8: Tax | | | | | | | | 0.022* | | |
| | | | | | | | | -0.012 | | |
| Subindex 9: Proactivity | | | | | | | | | 0.004 | |
| | | | | | | | | | -0.01 | |
| Subindex 10: Dispute Resolution | | | | | | | | | | -0.018 |
| | | | | | | | | | | -0.016 |
| Business Nationally Registered | 0.065 | 0.061 | 0.061 | 0.069 | 0.063 | 0.061 | 0.067 | 0.054 | 0.063 | 0.06 |
| | -0.048 | -0.048 | -0.048 | -0.048 | -0.048 | -0.048 | -0.048 | -0.049 | -0.049 | -0.048 |
| Business Provincial Registered | -0.038 | -0.024 | -0.023 | -0.013 | -0.027 | -0.023 | -0.029 | -0.025 | -0.024 | -0.019 |
| | -0.04 | -0.04 | -0.04 | -0.04 | -0.04 | -0.04 | -0.04 | -0.04 | -0.04 | -0.04 |
| Total Firm Assets in 2008 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Labor Size | 0.021 | 0.013 | 0.013 | 0.018 | 0.015 | 0.013 | 0.017 | 0.014 | 0.013 | 0.013 |
| | -0.018 | -0.018 | -0.018 | -0.018 | -0.018 | -0.018 | -0.018 | -0.018 | -0.018 | -0.018 |
| Growth in Sales (2006 to 2008) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Exporting Firm | -0.001 | -0.002 | -0.002 | -0.002 | -0.001 | -0.002 | -0.001 | -0.001 | -0.002 | -0.002 |
| | -0.003 | -0.003 | -0.003 | -0.003 | -0.003 | -0.003 | -0.003 | -0.003 | -0.003 | -0.003 |
| Percentage of Roads (Asphalted) | 0 | 0 | 0 | 0 | 0 | 0 | -0.001 | 0 | -0.001 | 0 |
| | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 |
| Distance from Ports (km) | 0.000** | 0.000** | 0.000** | 0 | 0.000** | 0.000** | 0.000** | 0.000*** | 0.000** | 0.000** |
| | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Provincial Literacy Rate (%) | 0 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | 0 | 0 | -0.001 | -0.001 |
| | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 | -0.001 |
| Sector Fixed Effects | YES | YES | YES | YES | YES | YES | YES | YES | YES | YES |
| Observations | 1106 | 1106 | 1106 | 1106 | 1106 | 1106 | 1106 | 1106 | 1106 | 1106 |
| Pseudo R-Squared | 0.0255 | 0.0197 | 0.0198 | 0.0244 | 0.0221 | 0.0197 | 0.0233 | 0.0221 | 0.0198 | 0.0206 |
| Chi2 | 38.02 | 29.3 | 29.47 | 36.3 | 32.92 | 29.27 | 34.71 | 32.88 | 29.45 | 30.62 |
| Log Likelihood | -725.2 | -729.5 | -729.5 | -726 | -727.7 | -729.6 | -726.8 | -727.8 | -729.5 | -728.9 |

Probit Model of Business Expansion. Marginal Probabilities with Robust Standard Errors, clustered at provincial level, in parentheses; *** p<0.01, ** p<0.05, * p<0.1; Dependent Variable is whether or firm will expand business over next two years, derived from collapsed likert scale.

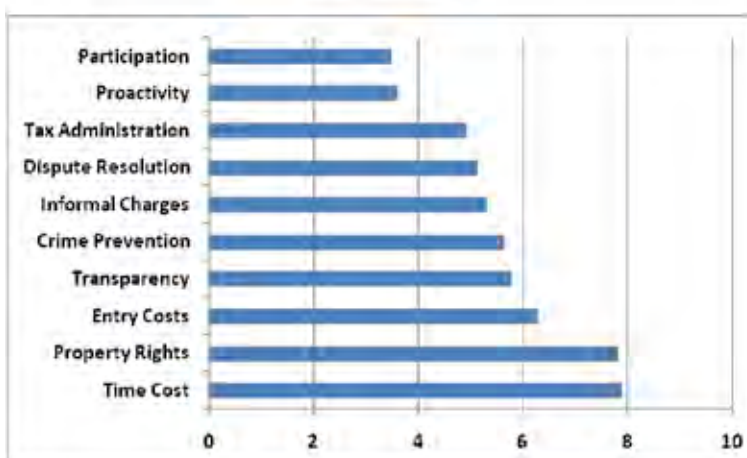
Appendix 5: Sub-indices by Province

Sub-indices are ranked from the weakest on top to the strongest at the bottom

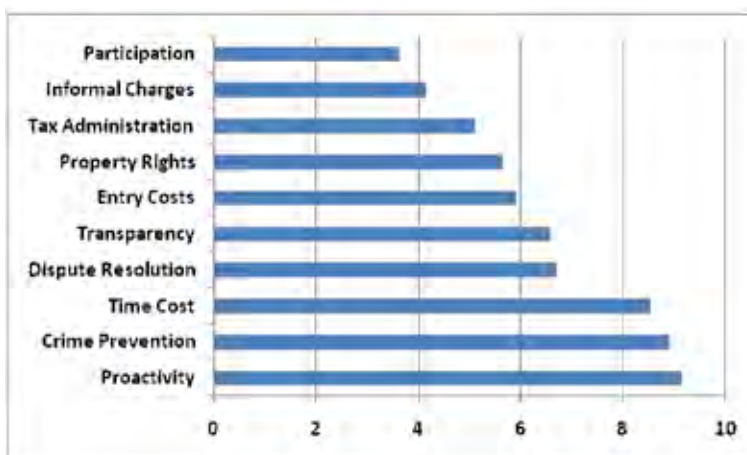
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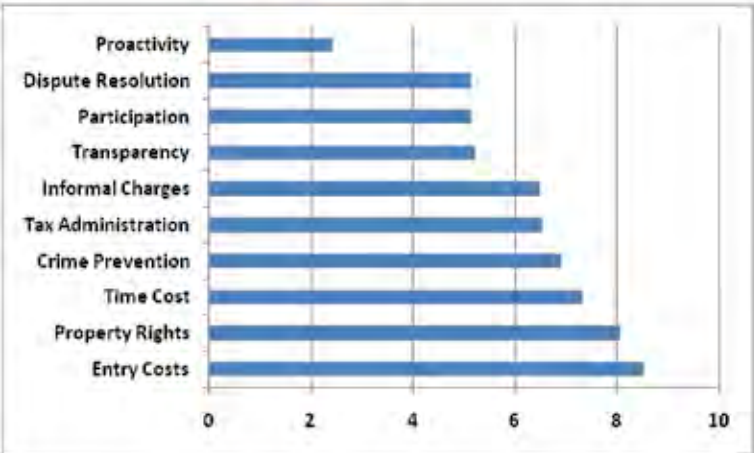
Battambang



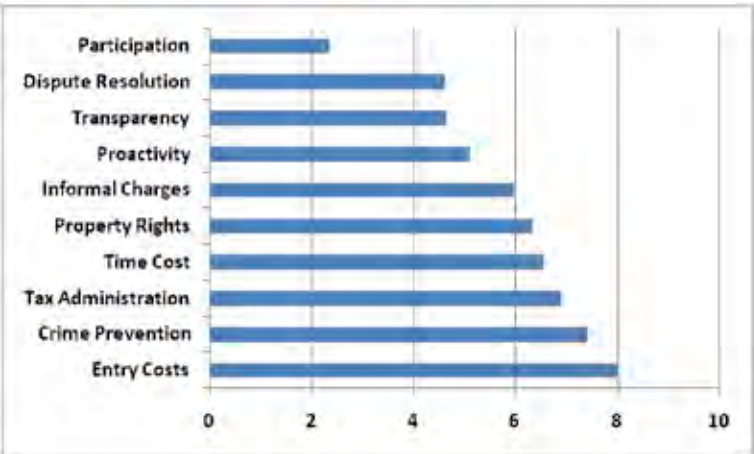
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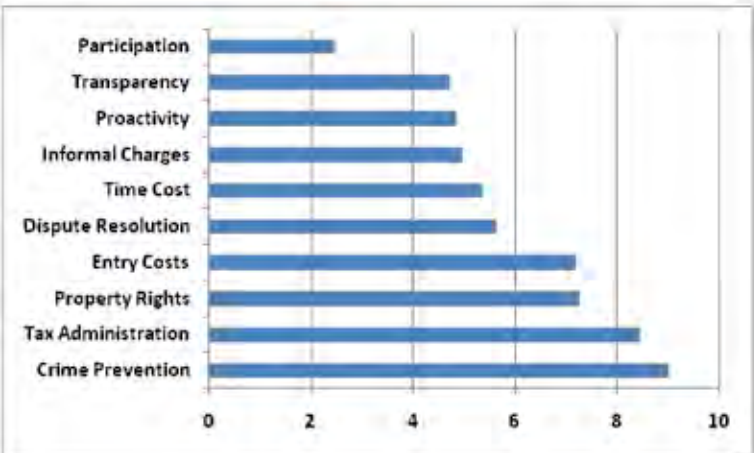
Kampong Chhnang



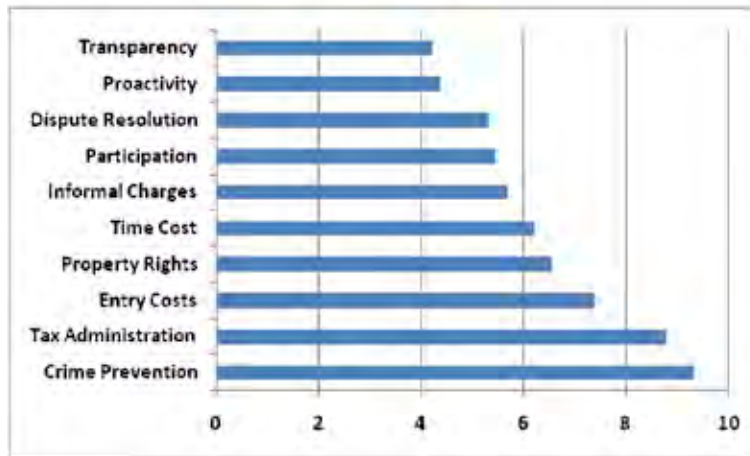
Kampong Speu



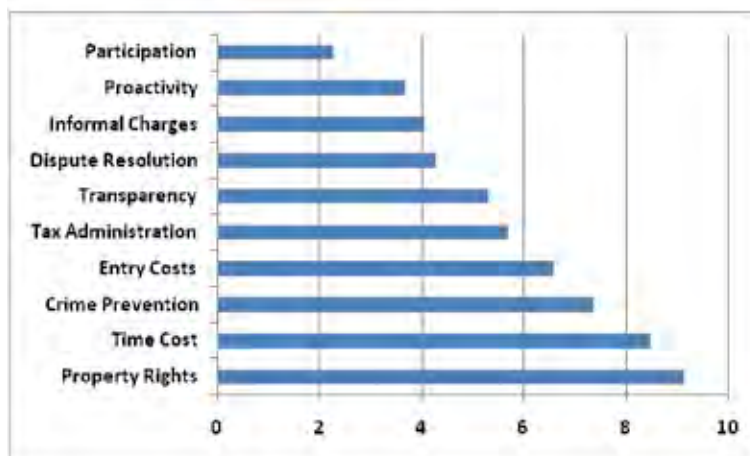
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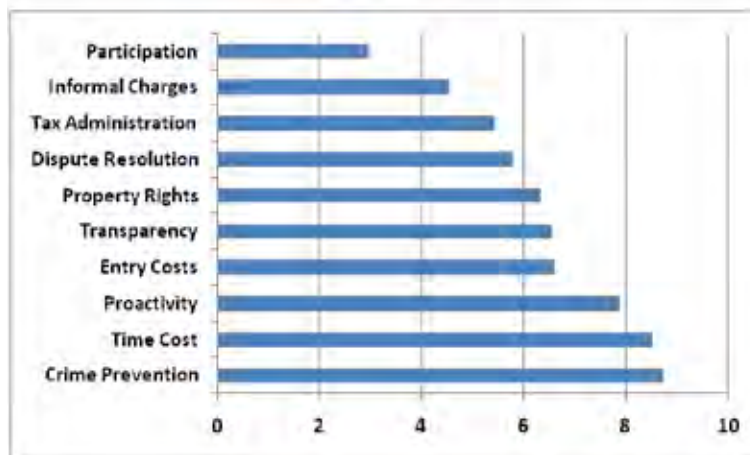
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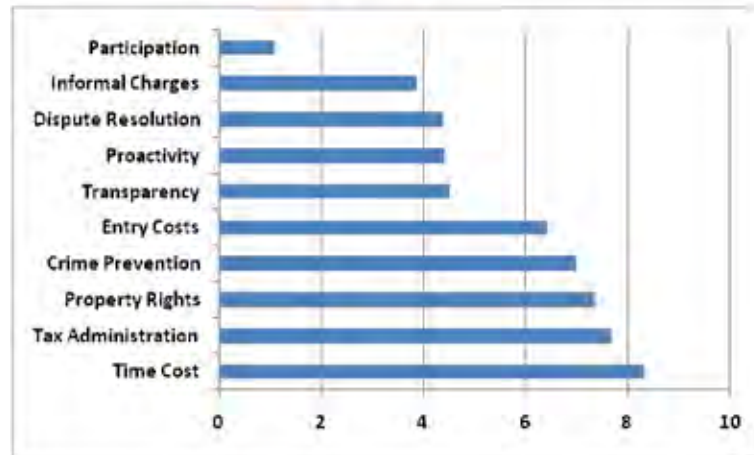
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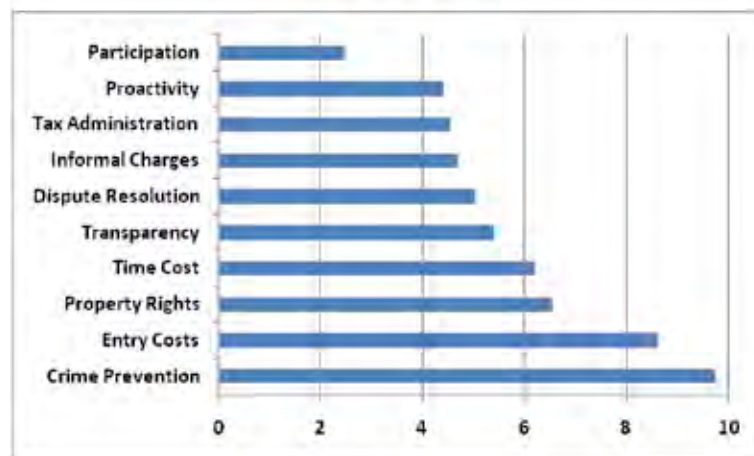
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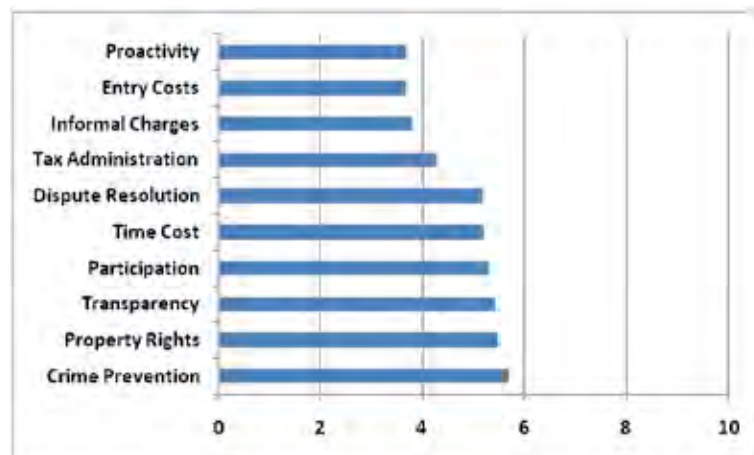
Kratie



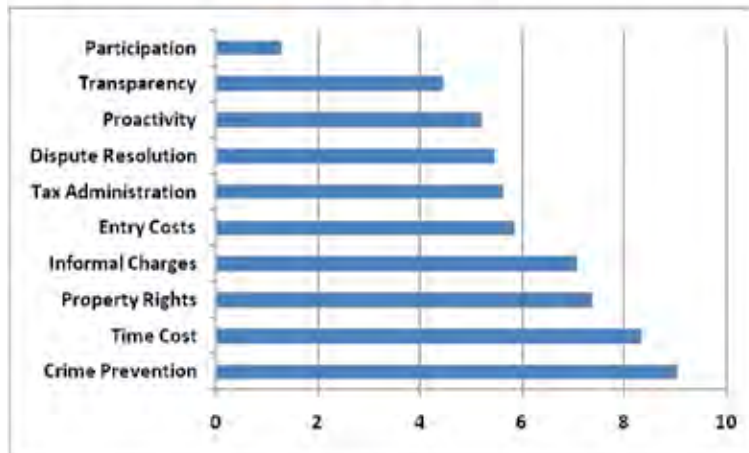
Mondulhiri



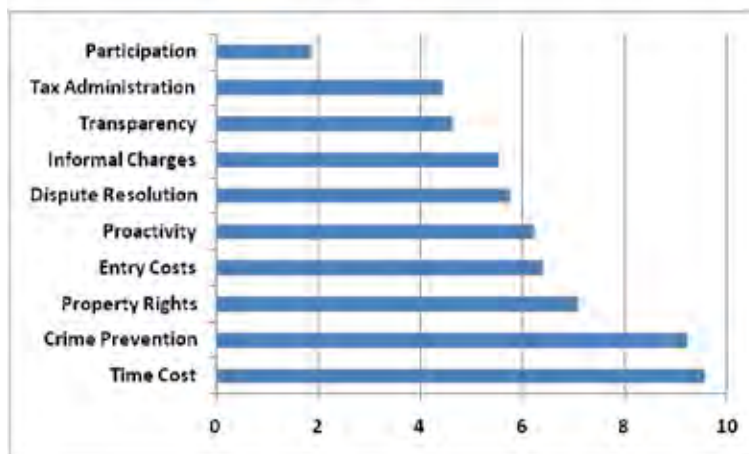
Phnom Penh



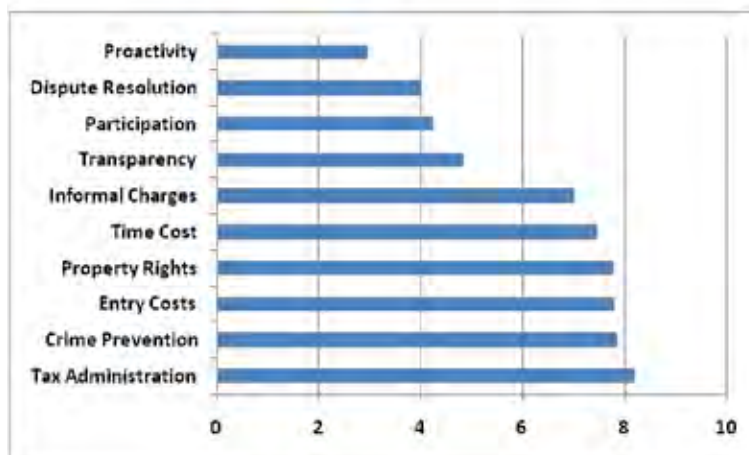
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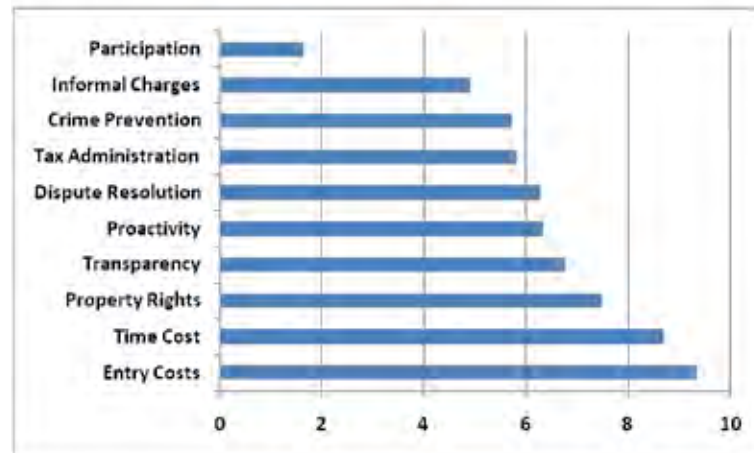
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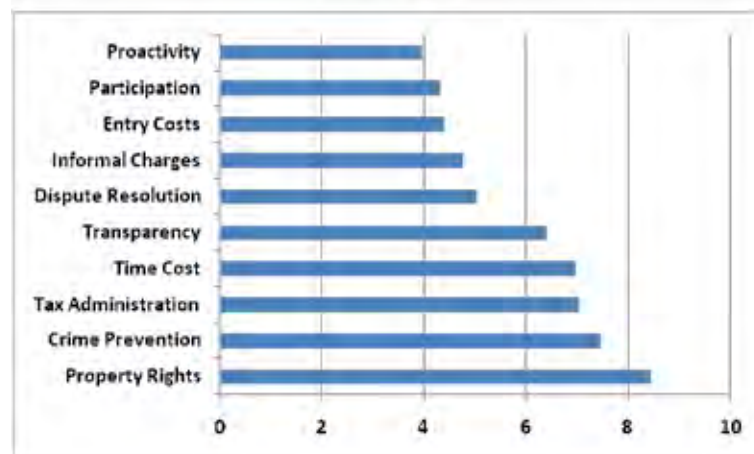
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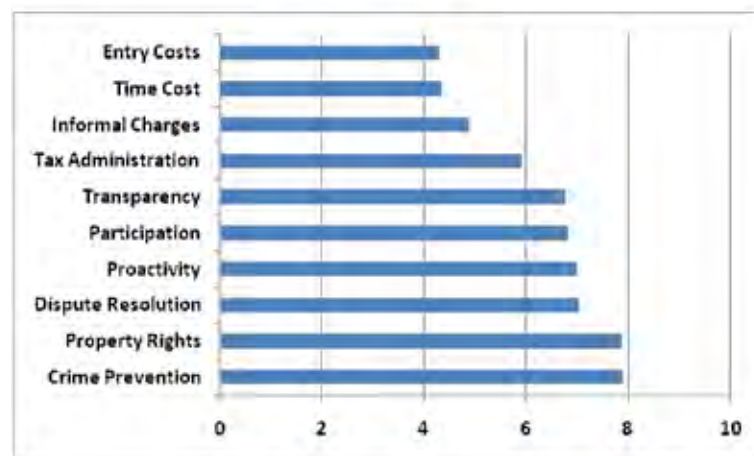
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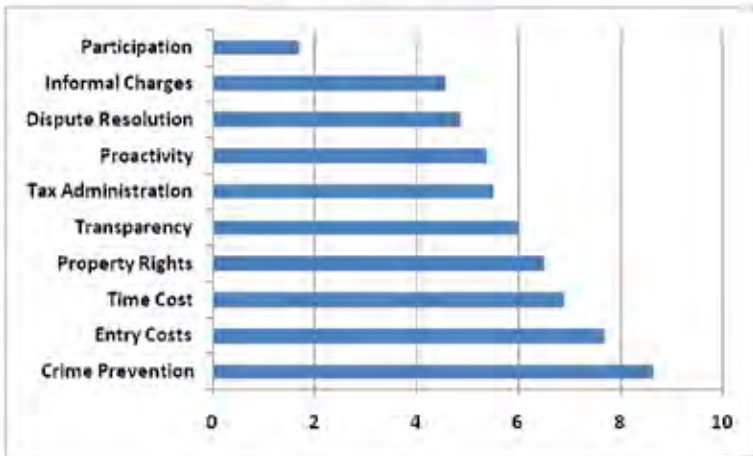
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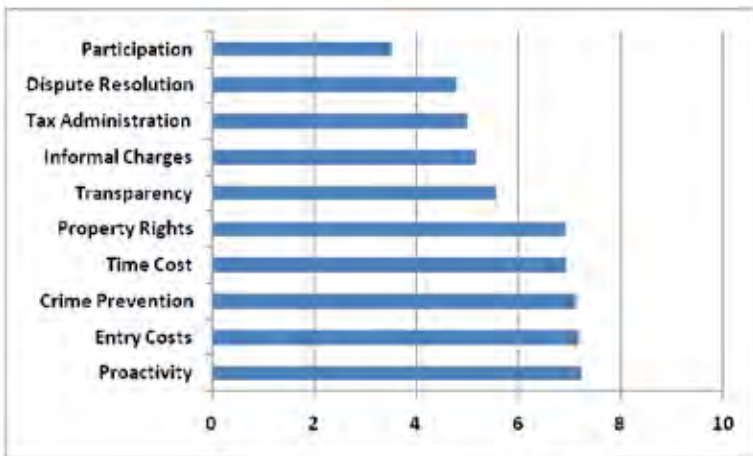
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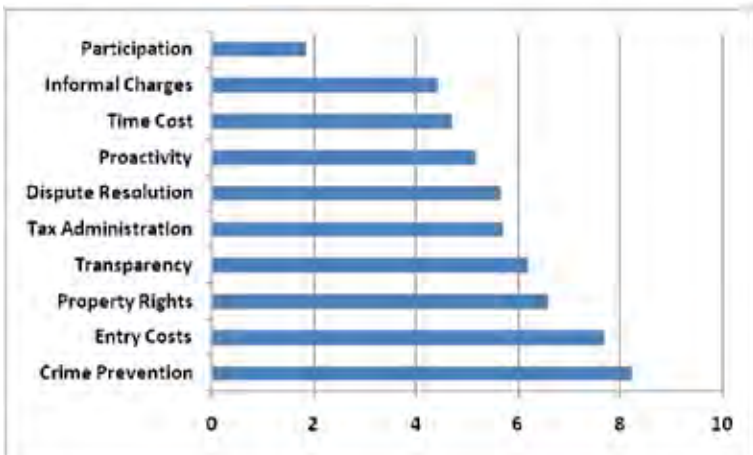
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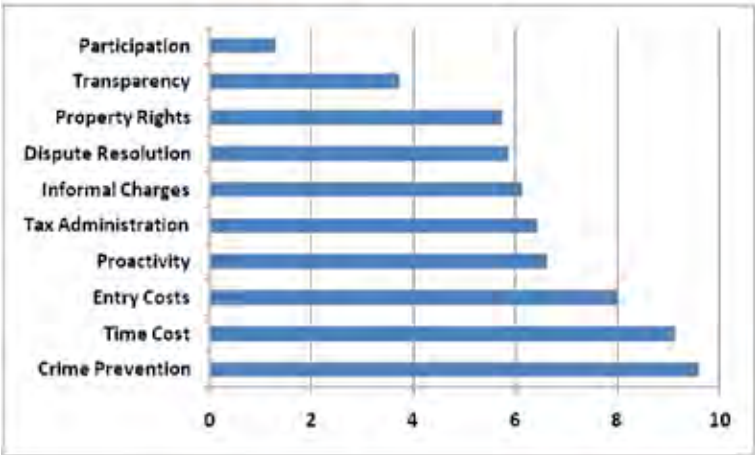
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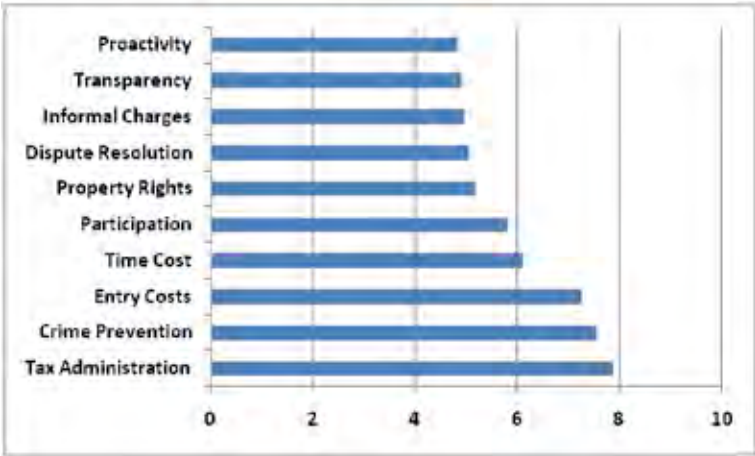
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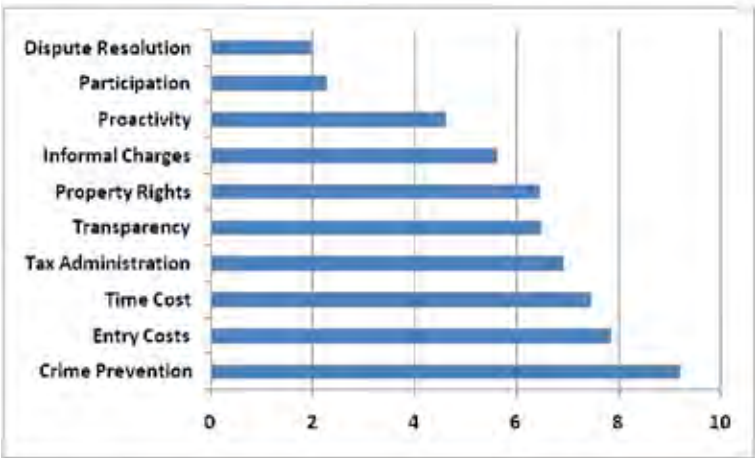
Oddar Meanchey



Kep



Pailin



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