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**The Structure of Tax Governance and Compliance in
Cambodia**

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I. Introduction

The new age of public policy and economic frontier has recently commenced to account for expanded perspectives, not only developed western world, but the BRICs (Brazil, Russia, India and China) as well as the rest of the Asian world (Cox 2012). Therefore, conventional policy knowledge and practices, associated with western-influenced culture, has to rapidly adapt to appreciate emerging trends of different cultures and perspectives, especially in Asia and the second world countries (Mahbubani 2009). This discussion paper aims to bridge the current governance knowledge gap and issues in the area tax compliance policy of developing Asian economy, in the case of Cambodia, to examples of good and effective tax governance and compliance in the modern economies. The goals of the paper are to highlight domestic public policy decision-making gap and issues in developing Asian countries in term of tax compliance, which can be dissected and theorized relative to a modern perspective. Furthermore, the discussion paper strives to postulate comparative understandings of occurring issues in Cambodia, which international public policy agencies must be accounted for and conceptualized.

II. The Definition of Governance and Imperative Domains

The concepts of Governance:

Governance is defined as “The act or manner of governing; the act or office of governing, (Kjaer, 2004 p.3)”

Kjaer (2004) refines the definition of governance as the following:

“Governance refers to self-organizing, inter-organizational network characterized by interdependence, resource-exchange, rule of game, and significant autonomy from the state (Rhodes, 1997a P.15 in Kjaer, 2004 p.3)”

Rosenau (1999) further emphasizes the internationalization of governance as the legal grounds that reside in all domains of actions ranging from personal to national and international entities, hence the consequences of each action or control can be impacted domestically as well internationally. Hyden (1999) further advocates that governance can be an official or unofficial resolution of all involved parties under agreed legal grounds and political scenarios. Kjaer (2004) summarizes the core

definition of ‘governance’ as the establishment of many involved parties, governmental or non-governmental, that seek to unify an interest under common legal ground and political scenario - that can be domestic or international as well as unified network of conglomerated entities.

There are many definitions that can be found within the broad term of ‘governance’, thus a parameter must be established for this discussion paper as the new definition of ‘governance’ may not specifically define the action of government (Kjaer 2004; Considine & Lewis, 2003). Therefore, the term ‘governance’ in this discussion paper specifically refers to the actions of the state through the bureaucracy that formulate and carry actions that related to tax compliance in developing Asian countries.

III. Tax Governance Structure in Cambodia

The Cambodian tax public administration adopts a function-based internal organizational design with an extension of large and medium taxpayers department (MEF 2014). Therefore, the internal organizational structure uses business functions to emphasize strong market-approach in the public sector policy, but the extension in design also add the diversification that focuses on taxpayer segment-based approach that emphasize bureaucratic-approach (Araki & Claus 2014; Ministry of Economic and Finance 2014; General Department of Taxation 2007, 2014).

Table 1: Core Administrative and Support Functions of the GDT

Core Business Process Functions						
A. Taxpayer Services	B. Taxpayer Registration	C. Return Processing	D. Auditing	E. Debt Collection and Appeals	F. Large Taxpayer Department	G. Medium Taxpayer Compliance Management
Support Functions						
H. Reform on Management and Organizational Structure						
I. Human Resource Management						
J. Information Technology						

Source: GDT (2014)

This section will outline the major challenges in tax compliance and governance structure for selected core administrative tax functions and support functions of the Cambodian General Department of Taxation:

1. TAXPAYER SERVICES

The challenges that are associated with taxpayer service are the quality and timeliness of the service delivery in terms of information and support to taxpayers (ARAKI & CLAUS 2014). Firstly, many improvement programs such as tax education and services training are being implemented, however, there is no coordination strategy to synergize all the implementation in aligning with the main institutional objectives (IMF 2012a). Therefore, the budget allocated to these programs is improperly monitored and weakly allocated, hence slowing the progress in providing quality information and service to taxpayers in terms of poor administrative training and lack of published guidelines (IMF 2012b).

Effective numbers of staff responsible for taxpayer services, on an international standard, should be around 15 to 20 percent in ratio to the total staff, however, the current Cambodian officers responsible for taxpayer services account to be less than one percent of the total staff. Conclusively, poor training and insufficient amount of allocated staff hinder the quality and timeliness of the service delivery and effectiveness (Araki & Claus 2014).

2. TAX REGISTRATION

Taxpayer registration is considered to be one of the top priority of the tax system, because an effective registration system is wholly responsible for robust processing of all tasks including the number of taxpayers, return filing, amount of debt collection, and other assessment processes (IMF 2012b; MEF 2014). The tax registration system has focused on the Wide Area Network in order to communicate, store, and process important data and information between all. The responsible authority, the Department of Tax Services and Tax Arrears, has explicated improvement in the registration system to encompass 16 out of 32 branches, however, further improvement has been slowed due to limited financial resources and information technology capacity. Hence, the GDT's registration system does not cover all the

potential taxpayers thus hindering the ability to effectively assess the specific debts of particular taxpayer (MEF 2014; Crandall 2010).

Ineffective cooperation between other governmental entities also proved to be problematic in term of over- and under- registration, as the governmental entity responsible for business licensing does not report detailed or relevant business structure to the GDT, hence creating problematic and incorrect assessment of the business's placement in the tax regime thus incurring negative impact on the economic environment (GDT 2014; IMF 2012, 2013; MEF 2013; Araki & Claus 2014).

3. RETURN PROCESSING

The Law on Tax dictates that registered taxpayers, specifically corporate entities, should lawfully and autonomously file and report their revenue and tax return monthly to the taxation authority. However, a fair share of the taxpayers do not report, misreport, and intentional avoid their tax obligations by omitting tax return process or submitting false report that declare low revenue threshold and/or 'no activity' in order to optimize their profit (GDT 2014). This practice has given serious concern to the tax administration as it creates non-compliance environment and incentive to tax evasion, however, few programs have been implemented to effectively address the non-compliance issues (IMF 2012, 2013; MEF 2013).

The problems associated with this practice often arise from lack of qualified staff, high amount of information and data, financial resources, monitoring process, and low compliance cost (Tanzi & Zee 2000; IMF 2012a; Bird & Zolt 2005, 2011). The manual process of tax filing, accompanied by other limited tax functions, makes the return process slow and ineffective, hence the monitoring capability and assessment of most business activities is extremely low and inaccurate relative to the actual business performance (GDT 2014; Araki & Claus 2014).

4. AUDIT

Auditing is the core monitoring process in non-compliance and an effective compliance instrument in the tax system. Auditing is heavily dependent on the level of skills and training imparted to the auditors and other staff that responsible for the

correct assessment and monitoring of the tax return data and information (Harioka & Sekita 2007; Yaniv 1999; Allingham and Sandmo 1972; Alm 2012). The GDT has pushed for extensive training for auditors and other responsible staff. However, the auditing performance has been declining in the performance indicator and overall limited. There are no standardized guidelines and overseeing agents that monitor and steer auditors, hence auditors tend to utilize different non-transparent methods for assessment of risk and case selection (GDT 2014). Auditors tend to inadequately assess business data, while intentionally or unintentionally omitting many important indicators thus resulting in lack of detailed risk assessment with no formal plan and case selection (MEF 2014).

The availability of detailed business information and data is scarce and lengthy in acquisition for auditors due to numerous formal requests of particular departments and governmental institutions. Therefore, the auditing process is ineffective and inefficient as the lengthiness of data and information acquisition for each case. The enforcement effort in compliance of the auditing team would be extremely undermining in identifying risk of evasion at an early stage as well as formulating enough evidence to capture any practices of illicit tax avoidance and tax evasion (GDT 2014). The enforcement effort also tends to create dissatisfactions and confusion to taxpayers, specifically large taxpayer units, due to incorrect assessment of risk and amount of owing debt thus negatively impacting on the economic environment (Araki & Claus 2014).

The number of auditing, on the international standard, should be account to be at 25-30 percent as ratio to the total staff, however, the GDT's auditing staff only account for nine percent of the total, hence ineffective monitoring and assessment capability of the Cambodian taxation authority (ARAKI & CLAUS 2014; GDT 2014; IMF 2012; MEF 2013; Araki & Claus 2014).

5. DEBT COLLECTION

The revenue gap in Cambodia is still high relative to other ASEAN countries; however, the collection capacity is still low (ARAKI & CLAUS 2014). The assessment of amount of debt has been problematic due to limited auditing processes and availability of data and information, thus the Cambodian taxation authority

cannot fully assess the total amount of tax gap and revenue gap clearly and correctly (MEF 2014; IMF 2012A; Gerasimova 2008). The initial challenges of debt collection range from the limited assessment of debt, untouchable, disappeared debtors, illicit avoidance and evasion, and weak administrative collection capability. Therefore, the GDT's request for payment for some large taxpayers has been ignore or simply counteracted with false reporting (MEF 2014).

In case of legal prosecution of illicit entities, the Cambodian Taxation Authority must formally request the overseeing governmental institution in order to press charges on the act (GDT 2014). However, the lengthy process might give incentive for the illicit practitioner to disappear or pursuing different solution and/or negotiation to settle the case in a less severe manner (MEF 2014; McGee 2012). However, this process is seen as ineffective due to false assessment on the GDT's part or lack of awareness from the taxpayers. The challenge of debt collection incurs problem associating with the integrity and transparency of the Cambodian GDT, thus resulting in negative economic performances and trustworthiness of the economic environment in Cambodia (MEF 2014; Malkawi & Haloush 2008).

6 LARGE TAXPAYER DEPARTMENT

Large taxpayers are the main source of revenue for the Cambodian taxation authority as it accounts for more than 80 percent of the total revenue. There are about 3,487 taxpayers and 1,500 taxpayers of which are the largest taxpayers within the Country. This segment of taxpayers has been heavily reformed in order to address many collection assisted by the International Monetary Fund (MEF 2014; IMF 2012). 100 of the largest taxpayers account for 60 percent of the total tax revenue so they are often contain massive activities, complex connections and complicated globalized structures of each of the company (Araki & Claus 2014). Nevertheless, GDT contain no specialized groups of staff that can effectively and fully comprehend the amount of debt owned and correctly assess the amount of risk associate with this segment of taxpayers. The factors of debt collection are fully dependent on the auditors assigned to specific companies (GDT 2014). However, some companies have the privilege of indecent auditing, hence the amount of revenue in financial report, and tax return are not fully disclosed and transparent to the taxation authority (CDC 2012; MEF 2013)

The amount of staff assigned to this segment of taxpayers only account for seven percent as a ratio to the total tax staff, hence it fails to meet the international standard of 10 % allocation of top specialized staff. Furthermore, only 1000 of the taxpayers should be categorized in this regime, however, there are more than 3000 in Cambodia so the amount of staff allocated to this segment is extremely low in comparison to the international standard (Araki & Claus 2014; IMF 2012; ARAKI & CLAUS 2014).

7. MEDIUM TAXPAYER COMPLIANCE MANAGEMENT

Obligation of medium taxpayers are managed under the judicial power of the tax branch office, and the medium taxpayers account for more than 85 percent of the total taxpayers in the real regime (MEF 2014; Crandall 2010). The estimated revenue of the medium taxpayers is around 10 percent of the total tax revenue, as the effort to improve this segment of taxpayer has been slow and unchecked (MEF 2014).

GDT has estimated that more than 60 percent of the medium taxpayers do not file their tax return and 60 percent of the total filing medium taxpayers report 'no activity'. The performance and structure of the medium taxpayers are often omitted and scarcely measured, hence their tax return process and financial reports are extremely incomprehensible. The cultural and non-compliance factors create a massive incentive for tax evasion and illicit avoidance due to no formal measurement and assessment (IMF 2012; MEF 2014; Haines 2004; Kaplan & Reckers 1985). Thus, a major reform in public sector policy is needed to address this problem as this behaviour has negatively impacted on the large taxpayer departments (MEF 2014; Braithwaite, et al. 2007).

IV. Conclusion

The discussion paper aims to highlight the occurring issues in governance structure and knowledge gap in the Cambodian tax public administration, especially in term of tax compliance, relative to the standardized and modern governance structure of the tax administration found in western world. The papers emphasizes strongly on extreme differences in term of governance culture, rule of law, and qualification of human resource. The common themes surrounding governance culture encompasses lack of tax compliance culture found in the general public as well as small-medium sized businesses, comparing to the deficient internal governance structure that are

unable to deliver quality public services, consultation and clear compliance guidelines. The rule of law expressed in the discussion paper exhibit low enforcement rate, corruption, and higher incentives for tax evasion and illicit avoidance as well as overall inability to coerce large-scale tax abiding culture. The qualification of human resources pursue a part in the ineffective implement of strong and sound decision-making and policy-making process, as the public administration are unable to carry daily tasks smoothly, failure in communication, low qualification, and incorrect assessment of policy and law. Reform in governance structure and public sector policy are essential in the modernization of the Cambodian tax public administration.

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