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A Summary of Cambodia's WTO Agreement ¹

The Kingdom of Cambodia became a member of the World Trade Organization (WTO) on October 13, 2004 after nearly nine years of negotiations with other WTO members.

While debates still persist about the potential costs and benefits of Cambodia's WTO membership, Cambodian entrepreneurs know comparatively little about the potential opportunities and risks of Cambodia becoming a member of WTO.

In light of this information gap, MPDF, in cooperation with the Ministry of Commerce, has prepared a guide for Cambodian businesses to explain what WTO accession means for the major business sectors. The following is a summary of the Guide that briefly describes WTO, the major commitments made by Cambodia, and provides a preliminary assessment of the implications of WTO membership for Cambodia's trading environment.

I. What is the WTO

The World Trade Organization (WTO) is the only international organization dealing with the global rules of trade between nations. These rules are formed by the "WTO's agreements, negotiated and signed by a majority of the world's trading nations, and ratified in their parliaments."² Essentially, WTO contracts are legally binding contracts between member countries that set out commitments and rules relating to access to markets. These contracts are enforced through a dispute settlement system that has considerable legal and commercial authority.

Although the WTO legal system is extremely complex, its principles are simple. They include: non-discrimination among members, transparency of trade laws and regulations, special treatment for developing countries, the use of only tariffs only for protecting markets, and progressive market liberalization.

By joining WTO, Cambodia gains an enforceable, contractual relationship with almost every other nation significantly engaged in trade. It offers firm and predictable treatment for Cambodia's products and services in the markets of all other members. The terms of the contract are briefly examined below.

¹ Unless otherwise noted, the information provided in this *Bulletin* including statistics, conclusions and recommendations is drawn from the Ministry of Commerce and MPDF's *Cambodia and WTO: A Guide for Business* (2005). It can be obtained free of charge.

² World Trade Organization (WTO), (www.wto.org). Accessed on January 30, 2005.



The "Business Issues Bulletin" provides those interested in business issues with a short summary and analysis of a particular topic affecting the business environment in Cambodia, and exposure to different opinions held by various stakeholders on the topic.

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Cambodia sought rapid accession to WTO. The need for rapid accession was driven mainly by the 1 January 2005 deadline facing the garment industry, as the international quota regime governing trade in garments ended on that date. After that date, all WTO members, in principle, would have unrestrained and unrestricted access to the markets of other members. Being outside the WTO would mean that Cambodian garment exporters risked continued quotas on their exports, something that would have had a strongly negative impact on foreign direct investment (FDI) in the industry.

Apart from access to the world garment market on “most-favored nation” (MFN) terms, other expected benefits include access to the international rules based system of trade with MFN terms for all goods extended as a right; an improved domestic investment climate due to liberalization in the trade of goods and services; and access to low-cost drugs through the WTO declaration on the easing of patents for least developed countries.

H.E. Sok Siphana, Secretary of State of the Ministry of Commerce

Personally, I see two major reasons for joining the WTO. First, WTO membership means that Cambodia’s interests could be protected. Acting on behalf of its private sector, the Royal Government of Cambodia has the right to bring issues and concerns to the various mechanisms of the WTO for assistance and resolution. This can be done in two ways: if Cambodia feels that certain trade practices are unfair, it can lodge the complaint officially and expect to be provided with a transparent hearing; and more importantly Cambodia can protect its interests by helping to shape the future “rules of the game” in its favor.

Second, for Cambodian reformists, the process of joining the WTO and the subsequent period, has offered and will offer Cambodia a new window of opportunity for comprehensive national reforms. This is the chance to push through unpopular but necessary reform initiatives in all areas to ensure that Cambodia can grow economically, politically and socially alongside other countries in the Asian region and beyond. The Prime Minister, Samdech Hun Sen, has fully understood this and seized the opportunity to step up concerted efforts to try to pull Cambodia out of the vicious cycle of poverty.

Mr. Keo Rottanak, Director of the Cabinet of the Minister of Industry, Mines and Energy

I heard about WTO from the news media and political leaders. There were debates about why Cambodia, as a least developed country, should join WTO. I’ve heard two opposing views: one argues that WTO membership provides opportunities for our country to grow and the other that we are not ready for WTO because we cannot compete at Cambodia’s present stage of development. My opinion is that Cambodia is not yet able to benefit from WTO membership as we are still very weak economically. We don’t have many things to sell, since we are still an agriculture-based economy. I don’t feel that we can compete at the moment.

Mr. Laing Ly, General Director Medical Supply, Co. Ltd

II. THE CONTRACT: What concessions did Cambodia make?

The WTO contract that Cambodia has entered into is far reaching. It will influence Cambodia’s laws and regulations and that will, in turn, shape the way Cambodian businesses operate. The four areas of law and regulation that the WTO agreement will affect are: the general business environment, the trade in goods and services, and the protection of intellectual property.

2.1 General Business Regulations

Cambodia has committed to enact a number of general laws to conform to the WTO rules. Among others, the key laws concern commercial arbitration, commercial contracts, establishing a commercial court, insolvency, and competition. Many of these laws are supposed to be in place by early 2006.

2.1.1 Regulating Trade in Goods

The first thing that comes to mind when people talk about trade, is trade in goods. There are many provisions in the WTO affecting cross-border trade in merchandise. Some are important for Cambodian exporters, while others concern importers. Three provisions will have an impact on import practices at the border: customs valuation, import licensing, and pre-shipment inspection (PSI). PSI will not be discussed because eventually the government will have to phase this out when the capacity of the Customs Department improves.

(a) Customs Valuation

Cambodia is committed to implementing the WTO Customs Valuation Agreement by January 1, 2009. The WTO Customs Valuation Agreement requires that valuation should be the transaction value (the price paid by importers) that is listed on the invoice as opposed to other artificial values, as practiced today. Although Customs are entitled to add certain costs or charges to the invoice price, the process will have to be transparent and predictable. Moreover, importers are entitled to the right to appeal a customs valuation without fear of penalty.

The Department of Customs operates two valuation schemes in the calculation of dutiable values for import and export of goods. The first scheme refers to fair market value (FMV), whereby the valuator (Societe General de Surveillances) under the Pre-Shipment Inspection (PSI) agreement uses international prices to determine the dutiable value. The second scheme involves the Ministry of Economy and Finance (MEF) setting, minimum, or fixed dutiable values for certain products to be used by SGS and customs. Customs duties, excises and VAT are calculated based on these administered prices. For some products, SGS is required to use the pre-determined minimum value in cases where the pre-determined value is greater than the actual SGS valuation based on FMV or cost, insurance, and freight (c.i.f) value. For a small number of other products such as petroleum, fixed dutiable values are used irrespective of the value. The purpose of this scheme is to circumvent under-valuation of imported items and ensure that customs officials and importers duly perform their respective obligations.

H.E. Hang Chuon Naron, Secretary General, Ministry of Economy and Finance

Relevant to customs valuation are tariffs applied on imported goods. There are two types of tariff rates: 1) bound tariff rates, which are the maximum rates that Cambodia can legally apply if it wants to under the WTO agreement; and 2) applied rates, which are the rates that Cambodia actually levies on imported goods.

In general, the differences between applied and bound rates in Cambodia are small, with the exception of the few products shown in Table 1.

Product	Bound rate*	Applied rate*
Rice	40%	7%
Cashew nuts	40%	7%
Mangoes	40%	7%
Rubber	15%	10%
Fish	15% - 40%	15% or 35%

* excluding VAT rate of 10%.

Sources: Cambodia and WTO: A Guide for Businesses. MoC and MPDF (2005).

Cambodia's Good Schedules (http://www.wto.org/english/thewto_e/countries_e/cambodia_e.htm)

Ministry of Economy and Finance, Kingdom of Cambodia (2004). Customs Tariff of Cambodia.

While some other countries such as India have bound less than 75% of their tariffs, Cambodia committed to binding all of its tariffs when it joined the WTO. This means that importers will know in advance what the maximum tariff rates could be for any products they want to import into Cambodia. Cambodia's tariff structure is bound at four bands or levels: 0, 7, 15, and 35 percent.

Cambodia chose to opt for a relatively liberal regime and shortly before the negotiations with WTO began, Cambodia undertook a reform of its import tariffs. This reduced the number of tariff bands from 12 to 4, so that after the reform, most goods were charged a duty of either 0, 7, 15, or 35 per cent. In the process, Cambodia eliminated most of the higher tariff rates that had previously been applied. Sensitive items are subject to high tariffs or "tariff peaks", which provide support either for nascent industries or those in need of transitional support while they restructure.

Cambodia agreed to implement its tariffs upon accession. It bound 100% of tariff lines, which effectively set ceilings on the tariff rates of all imported products. The agreed levels of the binding were, in all cases, equal to or greater than the level of tariffs that were actually applied in 2003. Thus, no significant reductions in tariffs below those set in the unilateral trade reform were required because of WTO membership.

H.E. Sok Siphana, Secretary of State, Ministry of Commerce

(b) Import License

Import licensing is permitted under the WTO, but only under tightly drawn conditions. Cambodia reserves the right to issue import licenses for five

2.1.3 Regulating Trade in Services

In effect, WTO's General Agreement on Trade in Services (GATS) is almost entirely about investment. There are few obligations that all members must accept. For the most part, countries take on only those obligations that they wish to, and in the services they are willing to open up to investment. Nevertheless, Cambodia's service sector is largely open, although general reservations and specific conditions apply to various sub-sectors.

In keeping with WTO principles, the GATS requires that countries must ensure transparency in the regulation of services and non-discriminatory treatment of foreign providers of services.

As the GATS is predominantly about investment, Cambodia needs to observe the disciplines (rules) under the WTO's Agreement on Trade Related Investment Measures (TRIMs). This prohibits investment promotion practices that could potentially distort competition. For example, investment incentives that encourage use of local inputs are banned.

In terms of market access for services, Cambodia adopted a generally liberal stance, welcoming foreign investment except in a very limited number of areas where local initiatives might be threatened. The negotiating team focused on areas that would contribute most to the investment climate by improving those services required by business. For example, Cambodia committed itself to allow foreign firms to operate in the areas of legal services (with some exceptions), accounting, auditing, bookkeeping, banking, management consulting, telecommunications and transport. In addition, Cambodia undertook commitments in areas that will help Cambodians develop the skills needed for a modern, competitive economy. Thus, it is committed to allowing foreign firms to provide higher education and adult education services. Also, Cambodia undertook commitments in areas it felt would contribute to improvements in health care and in the provision of sanitation, refuse and sewerage services, on the grounds that a foreign presence in these activities could contribute to improvements in public health.

H.E. Sok Siphana, Secretary of State, Ministry of Commerce

Of particular interest for the classes of products. Of particular interest for the economy are pharmaceutical and medical materials and agricultural inputs. Cambodia has, however, committed to eliminate quantitative restrictions on imported agricultural inputs by June 1, 2005. The other classes are weapons, explosives and ammunition; vehicles, aircraft and parts, ships, and boats, and other machinery for military purposes; and gold, silver, precious stones and articles made from them.

2.1.2 Regulation of Intellectual Property Protection

Increasingly, traded goods and services in the world are the creation of ideas and human ingenuity. To encourage inventors, they are given the right to benefit from their inventions and can prevent others from benefiting from them. These rights are protected by law and called intellectual property rights. The WTO agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) requires that members meet minimum international standards for the protection of patents, copyrights, trademarks, industrial designs, and others. Cambodia committed itself to fully implement TRIPS by January 1, 2007.

TRIPS will impact Cambodia's industrial development, in particular the pharmaceutical industry which remains nascent, and its growth will largely depend on long-term domestic structural reforms.

As required by WTO, Cambodia has passed intellectual property laws that conform to the TRIPS Agreement. If these laws are implemented properly, the Cambodian government will create a new environment that is conducive to trade, while still respecting intellectual property. Since this will reduce the amount of counterfeit medicine on the local market, WTO will help achieve positive effects on public health. In addition, the TRIPS provisions can also facilitate the transfer of technology and attract more investment in the pharmaceutical industry. This increase on the supply side should reduce the price of drugs and make them more affordable for poorer consumers.

Mr. Sok Hach, Director of the Economic Institute of Cambodia

four. The tariff commitments made by Cambodia are either at these levels or above them. Therefore, the immediate impact of accession on tariffs was minimal. The competitive effects of tariff reform have already been felt by domestic firms over the course of many years. However, many firms will feel the pressure of competition grow as the Cambodian economy grows.

Some recourse to help hard-hit domestic producers is allowed under the WTO agreement. This includes antidumping duties, subsidies, and safeguard measures. However, the conditions for such legal protection are strict, and the rules must be applied carefully. In particular, the government must prove that imports are harming domestic firms.

WTO will bring competition to the domestic market and this will impact local businesses that lack the human resources, financing and technology to become more competitive. We need more intervention from public institutions such as imposition of higher customs duties on imported products in order to protect local manufacturers and customs duty exemption on importation of raw materials and machinery. Recently, the Ministry of Economy and Finance has reduced customs duties on 458 raw materials imported for local production, but this exemption does not benefit our members, of whom 70% are in the food and beverage processing industry.

Mr. Heng Heang, Director of the Small and Medium Industry Business Association

3.2 Market Access Opportunities for Cambodian Companies

WTO accession will not significantly increase market access for Cambodian exporters. In fact, Cambodia, as a least-developed country, already benefits from favorable trade relationships with many countries. For countries where Cambodia does not enjoy preferential access, it enjoys “most-favored nation” (MFN) treatment.³ These preferential access schemes include the Generalized System of Preferences (GSP) scheme and the European Union’s “Everything but Arms (EBA)” scheme, which provide duty-free and quota-free access to least developed countries. Additionally, MFN treatment offers MFN rates, which are either WTO bound tariff rates, applied rates, or rates offered by members of a regional trade grouping to trading partners outside of the group.

WTO accession will help expand foreign investment in the banking sector, bring in new financial services to help strengthen banking activities, create jobs for university graduates and contribute to GDP growth which is part of government’s strategy for poverty reduction. In addition, WTO will help increase public confidence in the banking sector and Riel currency. This confidence will help the Royal Government of Cambodia to realize its de-dollarization strategy.

Nonetheless, WTO will bring competition for local banks because they lack capacity and capital and a competitive environment. This will cause them difficulties in a competitive environment.

The National Bank of Cambodia has considerably liberalized the banking industry without imposing any discriminatory or protective actions. Along with the efforts to strengthen banking services, the NBC has conducted investigations and enforced laws and regulations relevant to the banking sector and participated in the development of accounting standards for banks. We are also developing a leasing law with the support of the Asian Development Bank (ADB) in order to make it possible for small and medium enterprises to get the financing they need for machinery and equipment.

Another achievement recently is the establishment of NBC branches in the provinces and municipalities to facilitate the transportation of cash and payment of tax by businesses.

Mr. Neak Sarin, Deputy Director of the Economic Research Department of the National Bank of Cambodia

III. The New Trading Environment

These regulatory, investment, and trading commitments will affect how Cambodia does business after becoming a member. Together, these commitments create a new trading environment that Cambodian businesses will have to adapt to in order to compete and succeed.

3.1 Competitive Pressures from Imports

Competition in the domestic market may not intensify much as a direct result of WTO membership. During the process of joining the WTO, Cambodia reformed its tariff structure. As stated above, those reforms reduced both the average level of import duties from 17.4% to 16.5% and the number of tariff bands from 12 to

money to cover cash flow (both for sales credit and purchase of inputs in order to meet demands). There is a market for my products as our prices and quality are competitive.

Mr. Laing Ly, General Director of Medical Supply, Co. Ltd.

3.3 Dealing with Non-Tariff Barriers

While preferential treatment in many markets does give Cambodian entrepreneurs reason to be optimistic, there are many technical barriers that Cambodian exporters will have to overcome before their products can enter foreign markets. These include food safety standards and rules of origin. In addition, many markets will also require exporters to meet environmental and social standards.

While WTO regulations concerning technical barriers apply universally for all WTO members, food safety standards can be market specific. Countries are allowed to set higher levels of protection for the safety of humans, animals, or plants. Hence, the challenges are to understand what technical standards apply to which market, and ensure that Cambodian products meet those standards. Detailed information on standards of other WTO members can be obtained from the Camcontrol Department of the Ministry of Commerce.

Examples of products that have to face stringent food safety standards while enjoying favorable tariff treatment are fish and fish products. The EU, US, and Canada all offer duty-free market access for Cambodian fish, fish preparations, and fish pastes/sauce. However, meeting technical and health regulations in these markets can be extremely difficult. SPS regulations in the US and EU are stringent and complex, making export of fish and fish products to these markets very difficult at Cambodia's current stage of technical capability.

Rules of origin can be a barrier in some markets. These require that a certain percentage of inputs are sourced in Cambodia. As Cambodia imports many of its inputs, satisfying rules of origin can be a challenge. More information on this issue can be obtained from the Export Promotion Department of the Ministry of Commerce.

Cambodia enjoys preferential treatments in the region, particularly AFTAs (Common Effective Preferential Tariff (CEPT), and the ASEAN-China "early harvest" initiative. Bilateral preferential treatments are also offered by South Korea, and Thailand. These initiatives offer very favorable tariffs. For most products covered by these initiatives, tariff rates are zero. Furthermore, Cambodia benefited from MFN treatment from many other countries, even before becoming a member of WTO.

The mango is an example of a product that benefits from preferential treatment. Under the EBA scheme, the European Union's tariff rate for Cambodian mangoes is zero.

Similarly, Cambodia can export cashew nuts duty-free to most major markets (US, EU, Japan, Canada, and Australia), primarily because there is no direct competition in those markets. Under the ASEAN-China "early-harvest" initiative, Cambodian cashew nuts face zero tariff rates in China.

Through WTO, Cambodian businesses will have access to foreign markets. Along with this market access, there are challenges such as competition and the requirement to meet product quality standards. Cambodian businesses have limited understanding of quality standards and sanitary and phytosanitary (SPS) measures. They have not set up quality control systems which could help enhance sales in foreign markets. The government has yet to set up a quality control center to help businesses achieve quality standards. In addition, Cambodia does not have adequate infrastructure such as ports and roads to facilitate exports.

I have observed that the government has streamlined procedures and reduced barriers to competitiveness. But the government must continue to improve laws and regulations as well as enforcement in order to attract more capital and foreign direct investment that will expand the production base for export.

Okha Nang Sothy, Director General, Cambodian Chamber of Commerce

At the moment, I don't export my pharmaceutical products in any substantial way. Maybe I will in three years time. It's not easy to export. You need enough

Meeting such standards alone, however, will not ensure success. Cambodian products have to be competitive relative to those of other countries. This encompasses capitalizing on Cambodia's reputation as a country where international labor standards are observed, differentiating Cambodian food products as grown with little or no commercial fertilizers or pesticides, and reducing transaction costs.

The success that the Cambodian garment sector has had in creating a niche market for itself by ensuring high labor standards is commendable. This approach could be expanded to other sectors of the economy to further enhance Cambodia's reputation as country committed to high labor standards.

Our entrepreneurs do not have the capacity to access foreign markets due to quality control issues. Our organization has endeavored to encourage all members to improve quality in order to gain the confidence of consumers. This could help us compete with foreign products. The government should establish a product certification center in partnership with relevant foreign organizations.

Mr. Heng Heang, Director of Small and Medium Industry Business Association

I feel that WTO membership will affect Cambodian SMEs substantially as they cannot compete solely based on price in the new trading environment. Cambodian businesses face high costs for fuel, electricity and transportation.

Difficulties in competition don't come from Cambodia's membership in the WTO. But rather come from neighboring countries that are not members of WTO and have little regard for the laws of Cambodia. Vietnamese traders buy raw cashew nuts without paying any taxes while I have to pay 1% turnover tax. If I sell cashew nuts domestically, I am subject to another 10% VAT. If they compete on an equal playing field, I am ready to compete. But, the authorities take no action to address these problems. Hence it is very difficult for us to compete domestically when they again re-import to Cambodia without paying customs duties. Internationally, my strategy has been to compete based on the quality of my products. I provide high quality cashew nuts that

meet international standards in the "organic" niche market.

Mr. Banh Leng, Director, Khmer Agricultural Products Import Export Co., Ltd

There are an increasing number of consumers, particularly in the EU, US, and Japan who want to consume "organic food." They are willing to pay more for food that does not contain toxic residues. Many Cambodian food products such as rice, peppers, and others could sell in the niche market for organic food. What is needed is a facility for certification.

This strategy of selling to niche markets can be successful as long as the prices of Cambodian products are competitive. At present, this is not necessarily the case as Cambodian businesses face high costs of doing business, especially those brought about by bureaucracy. The extent of the costs vary according to sector and size of company. In general, however, the sectors that export their products incur the highest transaction costs when dealing with public officials. This makes Cambodian products less competitive.

Currently, Cambodia has few products for export, but I have observed that Cambodia produces a number of products which are not available in other countries. These products include handicrafts, fruits and palm products such as crystallized palm seeds. Our winning of IFC-MPDF's Corporate Citizenship Award in the area of environmental stewardship has made our products more saleable to customers in overseas markets.

The government should negotiate with other WTO member countries for trade preferences such as tax exemption or lower tax rates for Cambodian products. It should also remove barriers to competitiveness such as high costs for licensing. Cambodia is classified by the EU as a least developed country and will benefit from a low or even no import tax for products if they are made in Cambodia. To gain this advantage, we need to get a certificate of origin (C/O) from the Ministry of Commerce, but we must pay a fee for every export and customs clearance. This increases the costs of our products and makes us less competitive. I have noticed that the government has improved the C/O process and reduced import-export procedures to help the private

sector, but more concrete actions are needed from the government to improve the business environment such as establishment of a real “one-stop shop” for export.

Mr. Ly Aun Hay, Director of Confirel

The opportunities for organic foods in many countries such as the European Union, Hong Kong (China) and Australia were open before Cambodia joined WTO. The issue is that Cambodia does not have enough foreign direct investment in agro-industry which could lead to development in this sector. I believe that the WTO is good since it will help the government to attract more FDI, in particular to agro-industry.

Mr. Adisorn Chieu, Manging Director of Angkor Kasekam Rongroeng

Above all, it is important for Cambodians to know that Cambodia has some exportable products, especially agriculture products, which can command premium prices. What is needed are strategic and systematic approaches to ensure that products are competitive and meet the specific demands of their markets.

In my view, the Government will have to do whatever it can to build the capacity of its young private sector. New monetary and fiscal incentives must be provided, along with eliminating the cumbersome administrative burdens on the private sector. The Government has to be more pro-active and aggressive in defending the interests of the private sector. To be able to do this, the Government must first help build itself and its institutions. This is very critical as a weak government is always a real liability for the private sector.

Under the leadership of the Prime Minister, the government has embarked on a wide range of reforms to build the capacity of both private and public institutions and meet regularly with the private sector to solve problems and understand the needs of the private sector. The Government has also introduced a series of reforms and new legislation relating to the protection of innovation and creativity (trademarks, copyright, patents etc.).

The most important thing the Government has to do is ensure that its reform initiatives will be implemented in full. Among these are administrative, legal and judiciary reform and institution building. Institution building is not the building of one institution that happens to be at the forefront of a particular initiative. This reform must be seen in its totality by trying to address issues as a system.

Mr. Keo Rottanak, Director of the Cabinet of the Minister of Industry, Mines and Energy

That the government needs to improve the trading environment has been discussed, time and again, by the government. So, there is nothing new. However, I feel that there are necessary conditions for a growing private sector that must be met. These include:

- *Public administration reform so that public administration is more transparent and effective;*
- *Fight corruption - this will depend on the effectiveness of the first reform. Reducing corruption will lower the costs of doing business;*
- *Provide affordable credit for businesses.*

Mr. Banh Leng, Director, Khmer Agricultural Products Import Export Co., Ltd.