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FORMALISATION OF MICRO-ENTERPRISES AND HOME-BASED BUSINESSES

Recommendations Echoing from the 2018 ASEAN Policy Dialogue on Starting up a Business



FOREWORD

Micro-enterprises are very popular in all ASEAN economies. Micro-enterprises provide the livelihood for hundreds of millions of people in the region. Most of the micro-enterprises are unregistered, thus contributing to the high level of informality in most of the ASEAN countries. There is a general tendency to encourage micro-enterprises to register, to promote business formalization and to reduce the size of the informal economy. This is aimed at promoting the growth of the micro-enterprises themselves and to promote an equal business environment for all types of enterprises. However, there is also argument that the incentive policy to encourage micro-enterprises to register should take into account the nature of the micro-enterprises, their own advantages and their needs of staying micro and informal, and the special characteristics of each economy.

Under such context, the 2nd Policy Dialogue on Starting a Business in ASEAN - “Registration of Micro-enterprises and Family Businesses – What, Why and How in ASEAN region”? was held on 2 April 2018 in Luang Prabang (Lao PDR). The main objective of the policy dialogue was to create a forum for sharing relevant policies, good practices, and tools and lessons learnt between Government agencies in charge of SME and of starting-up a business, private sector stakeholders, development organizations, research institutes in AMS with a view to facilitating the regulatory reforms, policy development, implementation of programs to strengthen the performance of informal micro enterprises, family businesses, either by strengthening the existing establishments or by registering as a formal entity. This is under the overall objective of regulation reforms, simplification and rationalization of procedures in starting-up business in AMS and in moving towards a more harmonized starting up procedures in ASEAN. The policy dialogue should contribute towards ensuring an enabling, progressive and facilitative business start-up eco-system.

Micro-enterprises targeted and captured in the Policy Dialogue are those economic establishments which are owned by one person or a family. They are not registered (or loosely registered), not in the form of formal legal institution, without legal status and thus being considered as informal. They often employ less than 10 employees and rely mostly on family members as workers. These informal micro-enterprises are sometimes referred to as family enterprises, economic establishments or household business in some AMS. They are generally referred to as informal micro-enterprises.

This publication aims at reflecting the voices raised and recommendations made at the Policy Dialogue. Hopefully, the publication will bring the voices and opinions further and into more debate and discussions at other regional and national forum, thus contributing to an increasingly enabling environment for the development of micro enterprises in ASEAN. The publication is prepared by Economica Vietnam in strong cooperation with colleagues from ASEC, GIZ, and OECD. We would like to express our special thanks and gratitude to all participants, panelists and speakers to the Policy Dialogue who have generously spent their times and efforts to share their inputs, viewpoints at the Policy Dialogue.

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*Why Micro-enterprises and Home-based
Businesses are Reluctant to Register and
are yet to Register?*

PERSPECTIVE FROM THE PRIVATE SECTOR



“...The sharp rise in bookkeeping costs, in tax payment, and too high costs related to complying with regulations on tax, social security, labor make micro-enterprises balk at the decision to become formal...”

Nguyen My Thuan, Can Tho Business Association
Vietnam

“...The procedures to register is too complicated, time consuming, and microenterprises like mine has to pay quite a high fee. Registration process is complicated due to various steps and different government offices (e.g. Ministry of Commerce, Ministry of Industry and Handicraft...) without any coordination between them. We do not see any benefit or incentives like tax breaks or reductions offered to us when formalized...”

Nut Samphois - Owner of LSV Industry Co., Ltd.
Cambodia

“...Many micro-enterprises feel comfortable with the current informal sector status. Legality is considered unimportant. They will legalize when seeing the need for cooperation with third parties like the government, banks, or the potential for market expansion growth and enhanced competitiveness...”

Rizal Fahreza, Founder of Eptilu
Indonesia

“...Registration will make micro businesses to be visible to government authorities, especially taxes, labor, food safety, environment protection, etc. They are likely to be visited more by Government inspectors, and thus are subject to higher costs. They are concerned that there are more obligations for them to be fulfilled as a result of registration than the benefits from it...”

Thuta Aung, CEO of HamsaHub Consulting,
Myanmar.

PERSPECTIVE FROM THE PUBLIC SECTOR



“...We want to encourage MSME, including microenterprises, to contribute to national development goal. Our goals is to increase voluntary tax compliance, broaden potential tax base. Thus, we want to promote MSME’s awareness about tax obligations. Our approach is to introduce competitive tax rates, simplify book keeping and simplify tax payment procedures...”

Sulistyo Wibowo, Ministry of Finance
Indonesia

“...The Government has introduced special registration procedure applicable to microenterprise through single window for registration. A wide range of incentives have been offered, e.g. income tax exemption, exemption from the coverage of the Minimum Wage Law, financing and special credit window, assistance in technology transfer, production, management training, and marketing assistance programs... These incentives are available to those who register...”

Anna Liza F. Bonagua - Department of the Interior and Local Government, Philippines.

“...Simplifying business registration procedures and regulations are important first steps. After registration, micro-enterprises need to obtaining other licenses like construction permit, food hygiene certificates, trade permits... We should not be distracted only by the issue of business registration. There are many other post-registration issues which are of no less importance and which need to be urgently addressed to encourage micro-entrepreneurs to register their businesses...”

Dr. Leeber Leebouapao
National Institute for Economic Research
Lao PDR.

“....As an enabler, the role of the Government is to create a low-cost, enabling, corruption-free business environment and to introduce fair, transparent and highly accessible incentives for micro enterprises and home-based businesses when they wish to register.....”

Phan Duc Hieu, Vice President, CIEM
Vietnam

How should Micro-enterprises and Home-based Businesses be Promoted in ASEAN? – Key Recommendations

Recommendation # 1: Policy interventions should be based on evidence and full understanding of the micro-enterprise. There should be a clear definition of informal enterprises, and a complete database on them. Policies, regulations and support measures should be formulated by taking into account the characteristics, the diversity, the heterogeneity of informal and micro enterprises and thus their motivation and desired incentives. Data, statistics and analysis on microenterprises help to identify the target group of microenterprises which need to be formalized, supported with the right measures.



“...We should start from a good definition and a good understanding of micro-enterprises. Most AMSs seem to lump micro-enterprises with small enterprises. A clear definition on micro enterprises need to be worked out. A database and statistics on micro-enterprises need to be put in place. There are limited in-depth researches and understanding on the informal microenterprises in most of the AMSs. Policies and regulations made should take into account the diverse characteristics of micro-enterprises ...”

Participants of Group 7, Breakout Session



“...A deep understanding of the characteristics and the needs of microenterprises are the pre-condition for the success of a Government program or initiative to support home-based businesses. For example, in supporting microenterprises to access to finance, we crafted a program that meet the very specific needs and characteristics of micro enterprises, agricultural businesses, community enterprises in Thailand. We can't have one-size-fit-all solutions to address the constraints faced by microenterprises due to the fact that microenterprises are highly diverse....”

Dr. Wimonkan Kosumas, OSMEP - Thailand

Recommendation # 2: Balance between the wish and objective of the Government for formalization and the benefits and affordability of micro-enterprises. It is important to have a clear and firm understanding and communication of the WHY to reduce informality? Mutual understanding between Government and the private sector on the overall effort of formalization and increasing formality of the economy should be the cornerstone. Any effort to improve business formalisation should be win-win for both the Government and the microenterprises.



Larger and unregistered home-based enterprises should be registered to ensure the level playing field, but should we coerce a subsistence micro-enterprise to register and make them subject them to all kinds of regulations, compliance costs that will probably drive them out of business eventually? It is important that there is a mutual understanding and shared view on the benefits of formalization between the Government and private sectors involved in business formalization..."

Participants of Group 1, Breakout Session

Recommendation # 3: Set goals and objectives that are appropriate and proportionate to the capacity and resources of micro-enterprises. Outline the goals and strategic direction of the registration process (e.g. reducing informality, improving general business environment, reducing administrative burden, increasing tax base, improving health coverage) as well as prioritized areas beyond business registration (requirements on capital requirements, bookkeeping and financial reporting, social contributions, inspection, specific permits beyond business registration...). It is important to adopt a comprehensive policy approach.



"...The formalization pyramid shows subsistence entrepreneurs at the bottom, then those that will formalize with motivation and persuasion, then those ready to formalize and formalized SME at the top. Policies towards a larger formal economy should therefore be comprehensive and integrated..."

Mr. Antonio Fanelli, Organization for Economic Cooperation and Development (OECD)



"...Make it light, make it simple. DICA has made efforts to improve the regulatory reforms through the Company Law, reform the registration procedures, and strengthen enforcement. It has worked. However, we should recognize the fact that many microenterprises are happy with the legal status and the size as they are now. They wish to remain informal regardless of the improvements in regulations and procedures. We need to have a comprehensive approach..."

Ms. Tin Aye Han, Deputy Director General, DICA, Myanmar

Recommendation # 4: Set appropriate and flexible and targeted interventions, let the market forces work and respect the business freedom of microenterprises. Policy interventions should encourage rather than coerce micro-enterprise and home-based business to register. Governments need to ensure fair business environment and to address market failures (e.g. large home based businesses avoiding to register to avoid tax payment and labor regulations) as well as to protect social interests (hygiene standards, food security standards, social security for workers, environment protection...). These must be linked with appropriate and reasonable interventions (incentives, strengthening law enforcement, introducing new policies or programs, tax policy and incentives e.g. lowering tax rates and simplification) and improve general business environment, removing the “grey area” in the policy-regulatory framework.



“...Let the market forces work. Let micro-enterprises choose the best legal business form that work the best for them. Forcing micro-enterprises and household business to register might not be a good policy. Micro-enterprises will voluntarily register their business once they see the benefits out of it. That is the key to sustainable of micro enterprises and household businesses...”

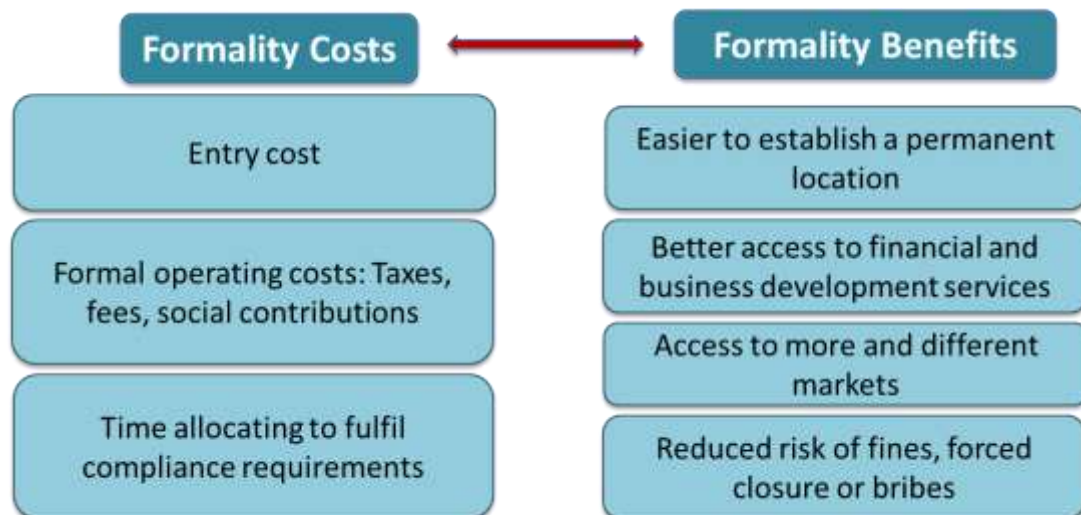
Mr. Phan Duc Hieu, Vice-President, Central Institute of Economic Management, Vietnam



“...Microentrepreneurs should have the liberty to choose the legal form for their businesses. But we cannot leave it all to the market. The Government should play the role of a facilitator. Governments can offer incentives, capacity building, and awareness raising. Government should also safeguard third party interests by making sure that microenterprises are subject to such regulations related to food safety, firefighting standards, labor security, fairness in the business environment. ...”

Mr. Mohd Rithauden Makip, Deputy CEO, SMECorp, Malaysia

Recommendation # 5: It is more effective to adopt a dual approach of reduction of formality cost (entry cost, formal operating cost, compliance cost, removal of “oppressive” and unnecessary requirements...) and increasing formality benefits (easier and cheaper to register, better access to finance, better access to market, reduced risks of fines, and of legal risks...).



Recommendation #6: Other than only business registration, regulatory reforms should also be focused on prioritized areas and in sectors. There are many other post-registration legal requirements, licenses, permits which micro-enterprises need to comply with and these need to be reformed as well. Regulations related to book-keeping and financial reporting, social contributions, inspections, construction permits, trade permits... all need to be reformed, streamlined in order to make the decision of micro-enterprises to go formalized a worthwhile and rewarding one for them.

“...We set a priority and put all the efforts to make a difference. We need to be focused on a priority area and we have chosen business registration. We made ceaseless efforts between 2014-2017 and Starting a Business Indicator of Brunei Darussalam jumped from 179 in 2015 to 58 in 2018. The reforms in business registration have encouraged thousands of entrepreneurs to register their business....”

Mr. Lim Sei Kee, Ministry of Finance, Brunei Darussalam





“...Charlie Munger said “intelligent people make decisions based on opportunity costs”. To further support the development of MSME, improving business registration is extremely important but simply not sufficient. There is so much to be done in supporting micro-enterprise to comply with other regulatory burdens, with social security, with labor standards, with tax regulations, trade permits... at the cost level which is reasonable and affordable to them...”

Mr. Peter Chen, Young Entrepreneurs Association Brunei

Recommendation # 7: Tax policy, tax incentives (lowering the tax rates, simplification of paying tax procedures) are highly necessary but non-tax incentive measures and support programs are equally important.



“...Complying with tax regulations are major burden for microenterprises to register. We think it is critically important to provide tax incentives to small enterprises when they register and to simplify the book-keeping, tax reporting and computation. Lowering the tax rates, easing and simplifying procedures to pay taxes, and raising the awareness of small enterprises to pay taxes will help to strengthen voluntary business registration”

Mr. Sulistyo Wibowo, Ministry of Finance, Indonesia



“...While tax incentives are important, it is necessary to understand the target audience and sector and to provide them with suitable non-tax incentive and support. From this perspective, SSM has adopted the “National Blue Ocean Strategy”. We see a tremendous impact of such non-tax support programs like SSM Online Networking Entrepreneurs, Youngpreneurs Go, Student Entrepreneurship Program and SSM Business Fair”

Ms. Norhaiza Jemon, Company Commission of Malaysia (SSM), Malaysia

Recommendation # 8: Involve multiple stakeholders in the process of supporting micro and home-based businesses, especially through innovative and participatory methods. Business associations are in a very good position to encourage microenterprises home-based business to register, and in advocating for effective policy and regulations, programs for business formalisation. Business associations should be engaged in the efforts of encouraging micro-enterprises to register, both at policy level and at micro level when it comes to direct support to micro enterprises.



“...Business associations are closer to businesses and should be the bridge between the Government and the microenterprises. Supporting micro-enterprises to formalize should not be the exclusive task of public institutions. Rather, it should be the important task of business associations and chambers. Business associations can help to improve the quality of policy, regulations on business formalization through their role as policy advocate...”

Mr. Dau Anh Tuan, Director General of the Legal Department - VCCI



“...Business associations are well positioned to advise microenterprises on the benefits of registering their business, of advising on the best decision that fit to their context, and on how to be prepared for becoming formalized. Business associations are simply one of the key players in the eco-system in support of business formalization...”

Mr. Ly Visal, Federation Associations for Small and Medium Enterprises of Cambodia

Recommendation # 9: A well-functioning eco-system (training, legal service, incubator...) in support of micro business formalization is highly important to facilitate micro-businesses to register. Key players of the eco-system need to be involved in the process when designing policy interventions and programs to support micro-enterprise to register or to formalise.



“...Having more microenterprises to register cannot be the task of one single Government or private sector institution. Establishment of well-functioning and effective business eco-systems is among the best ways to facilitate the formalization of micro and small enterprises....”

Mr. I Wayan Dipta, Chair of the ASEAN Task Force on Starting a Business

“...A strong eco-system to support micro-enterprises, a well-functioning network of business development service providers are among the key success factors for the business formalization and for the incorporation of unregistered businesses....”

Ms. Thiphaphone Phetmany, Laos Enterprise Development (EDC).



Recommendation # 10: Effective communication in support for business formalization is important. Effective communication can be achieved by making benefits of formalizing visible, tangible and understandable to micro-entrepreneurs through targeted communications/outreach strategies, based on context and real needs. This could feature public education, awareness raising campaigns, which are key for encouraging voluntary registration and for informed decision-making by micro-enterprises on formalization, based on true preferences and actual behaviours (and possible behavioural barriers) of the target audience.



“...Businesses are well informed about the benefit of registering formally with ACRA Singapore. Such benefits include recognition as legal entity to enjoy low income tax, ability to engage in financial services, secure IP and patents for new product and technology and safeguard business name and trade mark, liability protection to owners and shareholders, credibility and reputation, and perpetual succession ...”
Mr. Vincent Guee, ACRA, Singapore



“...Formalization brought about many benefits like access to information, market opportunities, market expansion, access to finance, government support programs, business connectivity... Once aware of such benefits through public education or awareness raising program, micro-enterprises will decide to register on a voluntary basis...”
Ms. Gemma Ngelangel, Gold Fish Brew and Brew, Philippines

CONCLUSION

The Policy Dialogue is “a forum for sharing relevant experiences between government agencies to strengthen the performance of informal micro enterprises and home-based businesses by registering as a formal entity” as put it by Mr. Timo Goosman, First Secretary of ASEAN Affairs from the Embassy of Germany to Indonesia. Mr. I Wayan Dipta, Chair of the ASEAN Task Force on Starting a Business appreciated the values of the policy dialogue. He added that “the policy dialogue really helps our work especially in terms of finding the best way to facilitate the formalization of micro and small enterprises towards improving our respective business eco-systems.”

It is true. The policy dialogue has been a forum, at regional level, for sharing relevant policies, good practices, and tools and lessons learnt between Government agencies in charge of SME and of starting-up a business, private sector stakeholders, development organizations, research institutes in AMS with a view to facilitating the regulatory reforms, policy development, implementation of programs to strengthen the performance of informal micro enterprises, home-based business and household businesses. What will matter more is the discussions and dialogues will be continued at national level at each of the AMS and be translated into policies, programs and actions to support the sustainable growth of the microenterprise sector and of the national economy.

The Second Policy Dialogue on Starting a Business in ASEAN, and with many more to come in the following years, will contribute to continuous public and private dialogue, persistent reform actions to the improvement of the business environment in ASEAN as a region and at each AMS, and to the achievements of the objectives and outcomes as articulated in the ASEAN Work Programme for Starting a Business.