

**TASK FORCE ON IMPLEMENTATION  
OF THE ENTERPRISE LAW AND  
INVESTMENT LAW**



# **REACHING A NEW HEIGHT**

## **IMPROVING THE QUALITY AND PERFORMANCE OF PRIVATE ENTERPRISES IN NEXT DECADE**

A Reviewing of Selected Policies which Affect the Performance of Private  
Enterprises

Le Duy Binh  
Pham Ngoc Thach  
Dau Anh Tuan

- Economica Vietnam –

*17 December 12 , 2010*

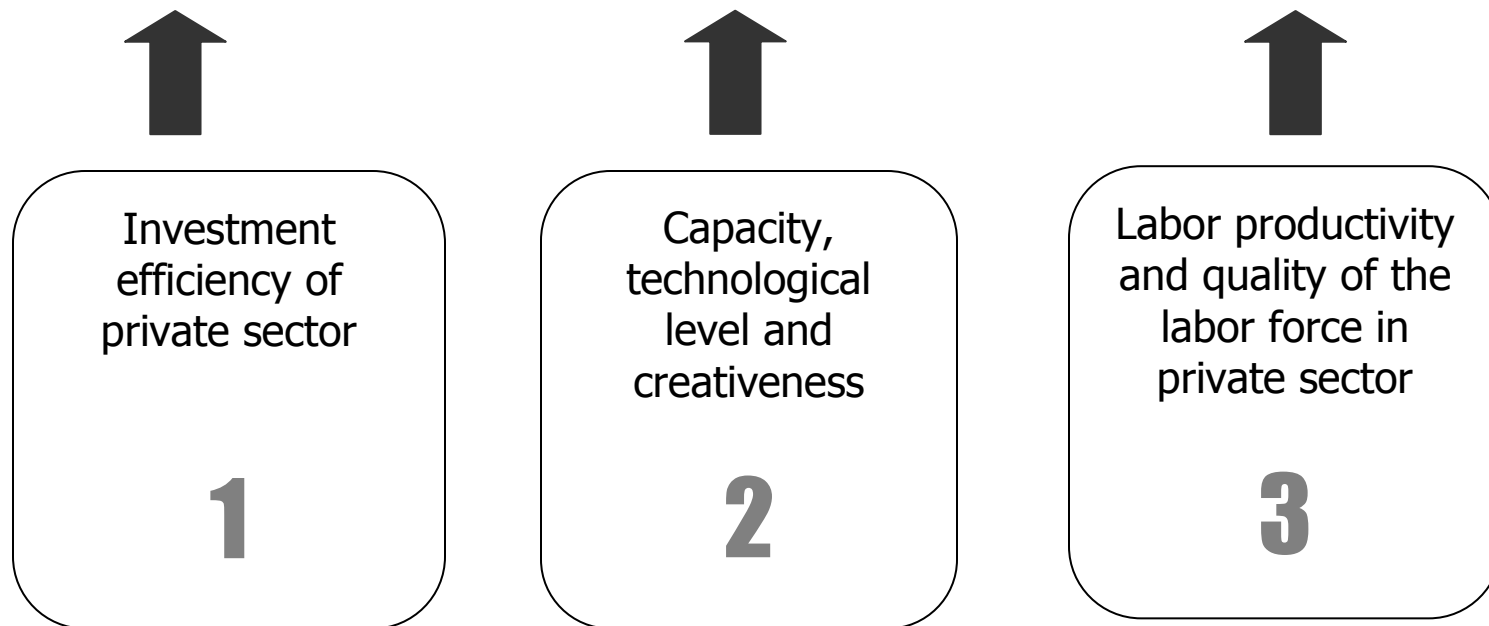
# The study

“With the objective of focusing on areas need improving and aiming at a sustainable strong private sector, satisfying new demands for development of the economy, this report does not mention policy achievements achieved”.

“Instead, the report emphasizes on analyzing current policy issues and providing specific suggestions to create breakthroughs in development, especially in quality and growth effectiveness of private enterprises in order to the development of an autonomic and highly competitive economy in the next decade”.

# Policy areas reviewed

## QUALITY AND EFFECTIVENESS OF PRIVATE ENTERPRISES



# **Part 1**

## **Investment Policies and Performance of Private Sector Enterprises**

# Some Figures....

- The number of enterprises registered rapidly rose to 415.000 enterprises (2009)
- Average charter capital was 1.29 billion in 2001, has increased to 11.16 billion in 2008.
- Financial performance indicators have been improved constantly over the years.
- While a State Owned Enterprise (SOE) needs VND 436.5 million of shareholder capital to create a job place (2008), an enterprise in FDI Sector needs VND 249.4 million, an enterprise in the private sector just has to make an investment of VND 224.1 million/job.
- Investment efficiency of private sector is higher than other sectors.
  - ICOR in 2007 of private sector is 3.74, lowest compared to other sectors (SOEs: 8.28; FDI: 4.99).

# Investment incentive policies laid a strong focus on emphasis on quantity development

- The freedom to do business was reiterated and materialized in the Enterprise Law, creating favorable conditions for the growth in quantity of enterprises and investment.
  - The strong growth is mostly in number and is to meet the urgent demands of the economy: job, income creation, export for foreign currencies...
- Policies and policies have been mostly focused on quantity objectives: 500.000 enterprises by 2010 and to create jobs.
- Success in quantity development is obvious. However, the strong emphasis on has led to some problems. Such a focus is no longer suitable to the new context of the economy.

# Unsuccessful in encouraging investment in high added value industries...

- The number of enterprises and labor mainly concentrates on industries that require low skills and capital, and that create low value added.
- Investment of new private enterprises are mainly made in labor intensive and low technology sectors. Investment in these sector accounts for:
  - 74.85% of enterprises
  - 86.2% of total labor
- The number of enterprises investing in areas which are deemed to use higher technology, requiring higher skills, or more capital such as finance, banking, training and education, scientific research, services, etc. only accounts for:
  - 19.5% of enterprises
  - 12.7% of labor

# Implementation of the role of in guiding investor behavior and encouraging investment

- The existing policies and regulation have not performed well the role of guiding or encouraging enterprises to invest in the way that best serves the economy's development objectives.
- Just 6.33% of enterprises operate in logistics sector: transportation, inventory, warehousing, information and communication, supporting industries (2007).
- Just 0.74% of enterprises registered to operate in agriculture, forestry, aquaculture – where over 70% of labors work and generate about 20.91% GDP of Vietnam.
- Number of enterprises investing in training and education accounts for 0.46% and in science is 0.03%, in health care is just 0.22%.
- 72% of enterprises locate in Red River Delta and South East Mekong Delta – a great imbalance among areas in the country.



# Implementation of the role of in guiding investor behavior and encouraging investment

- Investment policies failed to encourage or guide private enterprises to establish a strong supporting industry for large enterprises (for example FDI Enterprises or SOEs) or to become part of the global value chain:

*"...99% suppliers and sub-contractors for Canon Vietnam are FDI enterprises. Vietnamese enterprises in supporting industry mostly provide packaging services..."*

*– Mr. Sachio Kagayama, General Director of Canon Vietnam*

# Policies have not supported the sustainable and long term development of enterprises

- Financial performance indicators of private enterprises have improved over time.

<i>Return on Owners' Equity (ROE)</i>			
Private	<b>6.1%</b>	<b>7.1%</b>	<b>3.7%</b>
SOEs	13.2%	17.4%	13.3%
FDI	31.0%	29.0%	24.3%

- But the ROE has been dangerously low. The low ROE can be explained by the following reasons:
  - Private enterprises having limited accessibility to preferential treatment or market privileges which SOEs and FDI might have;
  - Lack of the the advantage of economies of scale...
- Low return rate signals that there will be many enterprises exiting from the market.
- It therefore cannot support the process of capital accumulation and reinvestment of private enterprises.

# Policies for encouraging the emergence and development of large private enterprises

- Prevailing policies remain “quiet” in motivating the development in size and scale of private enterprises and “quiet” in articulating the the importance of large private enterprises.
- According to the General Statistics Office, 1.44% of enterprises have capital of from 200 billion and above, and 0.57% have registered capital of 500 billion and above.
- In the report VNR 500 which ranks 500 largest enterprises in Vietnam, private enterprises only account for a small proportion.
- Large enterprises face some difficulties when restructuring to become a large corporate:
  - Restriction in advertising costs, brand development makes parent company cannot take on its roles well.
  - Subsidized companies are established, ensuring the autonomy and clear structure of the corporate. However, transactions among subsidies are considered transactions of independent entities. Thus the company are taxed many times.

# Policies and implementing investment incentives

- Policies and implementing investment incentives are different from international practices and have not received many positive response from enterprises
- Different documents provide many but scattered, uncoordinated incentives for enterprises. This confuses enterprises and results in low effectiveness.
- Forms of investment incentive are presented in a numerous number of complicated documents.
- The incompatibility among different regulations, policies in terms of incentive regime has reduced its effectiveness.

# Incentives in tax and land leasing fee is the most used policy instrument.

- Tax incentive is the easiest way for the policy makers when they wanted to introduce a new incentive policy. As a result, it is used with a high density in “a jungle of documents” issued and implemented by ministries, departments, localities in many areas.
- However:
  - A study by VNCI has revealed that just 14% of enterprises surveyed seriously studied tax incentives when making investment decision.
  - Another recent study in Binh Thuan also showed that about 12% of enterprises consider tax incentive is the most important factor to expand investment or start operation.
  - In the same study by VNCI, up to 56% of enterprises agree that policies, regulations on investment incentives are too complicated and incomprehensive, and over 50% agree that foreign enterprises receive more preferential treatment than domestic ones.
  - 78% of enterprises agree that “corporate income tax incentives is a nice gift, however it does not affect the investment decision of enterprises”.

# **Part 2**

## **Technological Application Level and Innovation Capacity of Private Enterprises**

# Some Figures....

- Global Competitiveness Report 2009 by World Economic Forum (WEF): innovation index of Vietnam is ranked 55/133; technological readiness index is ranked 73/133, Utility patents index is ranked 90/133.
- With about 480 private scientific and technological institutions, each has approximately 10 regular scientists, so now 4,800 scientists are working regularly in private sector.
- About 80 - 90% of the technology applied in Vietnam is imported, in which 76% of the machine, technological line dated from the 80s-90s, 75% of the equipments are depreciated fully, 50% of them are renewed.
  - There is no official number about the proportion of technology imported from source technology country, however the number of technology imported from China is estimated to be huge.

# Some Figures....

- The rate of enterprises with high technology is just 2%, whereas corresponding number in Thailand, Malaysia and Singapore is 30%, 51%, and 73%, respectively.
- According to the survey results of HCM Department of Science and Technology carried out in 2007 in enterprises which are located outside export processing and industrial zones, operating in 17 different areas:
  - Most of enterprises (over 60%) just invest to buy used equipments, machines. Of which, 81% has life of over 10 years, more than 22% of line equipments are not synchronic, at least 2% of the equipment need replacing completely; 25% of equipments needs overhauling and upgrading;
  - In terms of synchronism, 29% of the manufacturing lines are completely synchronic, 68% are relatively synchronic, and 3% are non-synchronized.



# Enterprises have not been encouraged to be creative and innovative...

- Protecting intellectual property right of enterprises and citizens has not been performed seriously, which eliminates the motivation for creativeness of enterprises.
- According to statistics of Ministry of Science and Technology inspector, in 03 years (2006-2009) 19,167 intellectual property right violation cases have been detected and handled (on average 532 cases/month).
- The creativeness level in enterprises is low:
  - By 2009, Intellectual Property Department has considered and granted the protection right to Vietnamese enterprises: 29 inventions, 45 useful initiatives, 747 industrial design, 16,231 trademarks.
  - A few number of technological transfer contracts including industrial designs are protected, accounting for 5% of the total number of contracts, which are mainly in manufacturing and assembling motorbike.
  - In 5 years (2004-2009), about 45% of enterprises have innovated products and 8% have innovated the manufacturing process.

# Imbalanced emphasis of policies

- Policies, legal documents has strongly affirmed the policy in encouraging enterprises to do research, apply and transfer technology:
  - Law on Science and Technology, Law on Technology Transfer, Law on High Technology, Law on Intellectual Property Rights and related Decisions, Technology Market Development Project...
- Policies put heavy emphasis on applying and transferring technology, has not focused on other areas need creativeness: innovate and change products, change methods, processes of manufacturing and management in enterprises.
  - Though machine and technology play important roles, they are means and cannot be separated from manufacturing process and know-how.

# Old thinking and methods still exist in policies and legal documents

- Similar to investment policies, tax and land leasing fee are two incentive forms that are common in investment encouragement policies in this field. There are no other new incentive way.
- There are some regulations which go against the spirit of Enterprise Law and are not suitable with international practices and market principles:
  - Clause 45, Law on Technology Transfer: “Annually enterprises can deduct part of the income before tax to set up a Science and Technology Development Provision, which will be used to do R&D and upgrade technology”.
  - Law on Corporate Income Tax states: “Enterprise is established, and operate under the jurisdiction of Vietnamese law can deduct maximum 10% of the taxable income per year to establish the Science and Technology Development Provision for that business”;

## **Old-fashioned way of thinking and mindset still exist in policies and legal documents**

- Strong intervention into the business of the enterprises:
  - “Organization and operation of Enterprise’s Science and Technology Provision Regulation” along with Decision 36/2007/QD-BTC dated May 16, 2007” specifies the establishment, usage and expenditure standard of the provision.
- The expenditure for technology innovation in enterprises on average is normally under 0.5% of the total revenue, much lower than the development requirement.
- As such, if policy makers think that those regulations are necessary, it should be applicable to state-owned enterprises only.

# Private enterprises with small scale find it difficult to access to incentive policies

- Similar to investment incentive policies, tax and land leasing fee are two incentive forms that are common in many documents. There are very limited other innovative incentive methods.
- Private enterprises normally cannot themselves organize and perform R&D activities due to their very small scale (98% of private enterprises are small and micro ones). Incentive policies do not take this important characteristic into account.

# High and Unreasonable Barriers to be recognized as a Technological Enterprises

- According to Decision 80/2007/ND-CP dated May 19, 2007 on Scientific and Technological Enterprises:
  - To be recognized as a technology enterprise, it should meet stringent requirements, e.g. the revenue from manufacturing and selling products made from the R&D activities in the first year account for at least 30% of the total revenues (TR), the second year achieve at least 50%, and from the third year at least 70%.
  - All over the country, there are 54 enterprises registered to operate in technology field, making up for 0.03% of total operating enterprises, and by now there has been 10 technology enterprises recognized (2008).
  - The number of staff, technician working in technological enterprises is 1,230 people, equivalent to 0.02% of total labor in private enterprises.

# Inefficient design and implementation of programs supporting the technological innovation

- Policies encouraging enterprises to do research, invest, operate in scientific and technological field, and innovate technology have been clearly defined in Decision 119/1999/ND-CP and Decision 122/2003/ND-CP of the Government, in which the amount supported by the Government can reach up to 30% of the total expenditure of the technological research, upgrade, innovation, and product manufacturing.
- However, from 2002 to 2009, Ministry of Science and Technology has approved 159 research topics (28% of total number of enterprises registered), 54% of which belong to SOEs, 45.9% belong to private enterprises.
- Procedures to review and approve technological innovation projects are too complicated, inconvenient, and through many stages. Not only the state capital but also the amount borrowed from the bank, which has been through the investment assessment by the bank, is reassessed by state management agencies.
- Information about government support program is scarce and difficult to access.
- The requirement to contribute 70% of the investment in technology projects is beyond the ability of many private enterprises.

# Policies promoting the development of technology market has not resulted in positive development

- Lack of model and motivation to develop supply and demand for the technological market
  - There has been not a specific policy to develop the supply of technology (companies, center, companies separated from institutions).
- Since 2002, Techmart has been organized annually at local or national level. Thousands of principle contracts to transfer technology with huge value (thousands of billion VND), however these contracts signed at Techmart are not implemented in practice.
- It is not possible for the majority of Small and Medium Enterprises (SMEs) to carry out R&D activities themselves. Incentive policies seem to ignore this characteristic of small businesses.
  - An efficient technology market will therefore of critical help for SMEs.
- From 1993 to the beginning of 2009, Ministry of Science and Technology had approved 701 technology transfer contracts which mainly belong to FDI Enterprises.



# **Part 3**

## **POLICIES AFFECTING THE LABOR PRODUCTIVITY AND QUALITY OF THE HUMAN RESOURCES**

# Abundant and cheap labor but enterprises still lack of labor – a sad paradox

- In 2009, private sector provides job for 85% of the country's labor force. The number of labor working in State owned and FDI Sector accounts for 11.5% and 3.4%, respectively.
- The labor force of the country is 47.7 million people.
- In 2009, 47.4% of enterprises surveyed by VCCI have difficulty in recruiting skilled labor (the rate in 2008 was 38.4%)
- In 2007, 70,4% of Japanese enterprises faced difficulty in recruiting Vietnamese technician, 63% found difficulty in recruiting middle management (this rate of ASEAN countries was 39.1%).
- 75% of the labor working in private enterprises are untrained.

# The existing labor structure mirrored the low competitiveness of the economy

- Labor structure represents the low competitiveness of the economy and the way to the prosperousness is still far away:
  - The number of labor working in technology field just makes up for 0.06% of total number of labor in the country, and of the enterprise sector alone, the number is 0.02%.
  - In 2007, 86.2% of labor work in private enterprises which do not require high level of skills or knowledge on technology.
  - Just 12.7% of labors are working in enterprises using higher technology and requiring higher skills.
  - Average productivity of Vietnam in current price was VND 34.9 million. Productivity in science and technology is the highest, with 395.8 million VND/capita in 2009.
  - The growth rate of productivity of Vietnam is low. On average, from 2000 to 2009, it was 4.53%/year. Especially, in 2008 and 2009 it was 3.21%/year and 2.89%/year, respectively.

# Vocational training quality

- Labor supply and demand forecasts have not been performed well and vocational training programs have not considered the real demand of enterprises and associated to the economic development policies of the local.
- Methods and implementation of training programs are not suitable to trainees.
- In 2001, 887.3 thousands people are trained; in 2008, 1,538 million people graduated from vocational schools.
  - However, the quality of vocational training basically has not met the needs of enterprises and the number and training structure still imbalance. Training structure among levels imbalances, the current state is "Abundant of masters, lack of workers." Training proportionate in Vietnam among universities and colleges - professional secondary education - vocational training is 10: 9.8: 30.3 (compared to other country is 1: 4: 10).
- In 2008, the World Bank (WB) assessed and scored the quality of Vietnam human resources 3.79 points (out of 10) - ranked 11th in 12 countries surveyed in Asia. The reports indicated that Vietnam lack of highly qualified experts, lack of skilled workers; knowledge economy index (KEI) is low (3.02 points, ranked 102/133 countries and territories.)

# Regulations on the percentage of mandatory courses and training modules

- According to Decision 58/2008/QĐ-BLĐTBXH, June 9, 2008, vocational college must ensure the curriculum framework of vocational college level meet 70-80% the requirements set by the General Department of Vocational Training (GDVT).
- From 2006 to 2009, the Ministry of Labor, War Invalids and Social Affairs has developed 164 frameworks for colleges, vocational training intermediate school .
- This regulation also shows the deep intervention in the training contents of vocational schools. The application of a curriculum for all schools without considering the difference between the local, the specific requirements of local businesses is unreasonable.
- The argument given was to ensure the quality of vocational training, protect the students' rights.
  - **However**, to this objective, General Department of Vocational Training should adopt other measures instead of current rigid ones. Quality of training and prestige of the vocational training institutions should be let to evaluated by the market.

# Strict regulations on worker lay-off

- Strict regulations on the lay off of workers reduced the mobility of the labor market. And actually, the measure has counter effect and fail to protect the workers.
  - Enterprises tried all ways they can to avoid signing official labor contract with workers, thus affecting the legitimate right of workers in terms of accessibility to social insurance, health care insurance, etc.
- Abrupt dismissal of workers always put the enterprise in a position that it will face a court case. This also reduces the flexibility and mobility of the labor market.
- Regulation provisions for cases eligible for lawful dismissal/ lay-off is few, far from practice and thus do not work.

# Some regulations related to the industrial relations is too far from practice (1)

- Tripartism in handling industrial relations:
  - ILO convention and laws of countries in the world have acknowledged the importance of this mechanism and considered it as one of the pillars of the industrial relationship.
  - The Vietnam Labor Code also recognizes this.
  - The two representative bodies of the employers in Vietnam are the Chamber of Commerce and Industry of Vietnam (VCCI), the Cooperative Union of Vietnam
  - But the two body have not performing this role very well.

## Some regulations related to the industrial relations is too far from practice (2)

- Right to go on strike :
  - A strike is recognized as lawful if it is on benefit-related disputes.
  - However, the lines between right- and benefit- related disputes are not clear.
  - The Labor Code emphasizes the role of the Trade Union in a strike. A strike can be only seen as lawful if the trade union is involved. But the performance of the trade union is very limited.
    - There are only 20.399 trade union operating at private enterprises (while the total number of private enterprises is now 500, 000) private enterprises.
    - As such, the regulation stipulating the mandatory organization and leadership role of the union is a major limitation for workers to exercise their right to strike in enterprises where no trade union has not been established. In other words, this regulation has made impossible for workers in more than 80% of private enterprises to go on strike in a lawful manner.



## **Some regulations related to the industrial relations is too far from practice (3)**

- Protecting the properties of the enterprises when the strike happens:
  - Many countries in the world and the International Labor Organization (ILO) consider the right to “lock-out” the enterprises as one of the basic right of the employers. This right is equal to the right to go on strike of the employees.
  - The current Labor Code has not included this right.

# Other unreasonable issues in Labor Law

- Many regulations of the Labor Code have created difficulties to businesses and reduced the competitiveness as well as the productivity and efficiency of enterprises:
  - Currently, equitized (privatized) enterprises still have to comply with some regulations in terms of payroll ladder stipulated by the Government.
  - The maximum permissible overtime work hour is 200 hours, much lower with other countries like Indonesia, Bangladesh, etc.
  - According to current regulations of the Labor Code, enterprises find difficulty in mobilizing labor to work overtime in special occasions, for example being in a hurry to meet the customers' orders in high demand periods like Christmas.
  - Unpaid leave period of employees is still included when calculating the severance allowance, which is unfair to enterprises and employers.
  - Costs related to recruit labor for vocational training, internship have not been tax exempted, as a result it does not encourage enterprises to actively participate in training activities.

# Regulations on social security are not implemented seriously

- Social security issues: Enterprises with good social security policy will help increase the productivity, efficiency, profits, competitiveness, and promote the sustainable development of the enterprise. However:
  - “At present, there are 33,000 enterprises out of 137,000 enterprises operating in HCM City pay social insurance for employees, accounting for 25%”.
  - “In 2009, Danang has 144,986 employees with social insurance being paid, equivalent to 70.5% of the total workers which are required by laws to be covered by social insurance.”
  - “In Hanoi, the rate of SME workers benefiting from social insurance coverage is 60.53%”.

# Enforcement of requirements on work safety and work conditions is weak

- Current Labor Code lack regulations in terms of standard setting, national standards and profile in industrial hygiene and safety. Regulations in organization, standards in technical safety and hygiene verification are essential but not yet stipulated in this Labor Code.
- Responsibility for paying salary as specified in the employment contract for employees having accidents at work, occupational diseases and taking leave for treatments, and paying the entire health care costs based on the degree of disablement should be specified in the Labor Code.
- The implementation of requirements in labor conditions should be enhanced:
  - According to report of the Vietnam General Confederation of Trade Union, in 2008 there are 5,836 cases of accidents in the whole country with 6,047 victims, 508 dead cases (573 dead people) and 1,262 injured people. Among accidents, the rate of electricity shock accounts for the highest (26.7% of cases), falling from high points (17.6%) and rolled by equipments, machines (5.7%).
  - According to reports by Ministry of Health, provinces has examined 12/25 types of occupational diseases for over 104,000 people, in which over 1,000 having occupational diseases (at the end of 2008, more than 24,000 having occupational diseases). Some diseases have high ratio such as lung related disease(74.1%), deaf because of noise (16.01%). Besides, over 6,800 cases of pesticide contamination, with 7,600 cases of contaminants, 137 death accidents were reported.

# The relationship between employers and employees

- Social dialogue and negotiation between enterprises and employees:
  - Rate of private enterprises having collective employment agreement is low. According to Vietnam General Confederation of Labor approximately 25% of private enterprises, 40% of FDI enterprises and 95% of SOEs have collective employment agreement.
  - In SME sector, as low as 10% of enterprises have labor union, in many enterprises the labor unions are very weak. They seem to act an “extended arm” of the employer. As a result, when dispute occurs, employees are not protected. Wildcat strikes are therefore a common place phenomenon.
  - According to statistics from Ministry of Labor, War Invalids and Social Affairs (MOLISA), from 1995 to July 30, 2009, there were 2,743 strikes nation-wide. Most of the cases happened in FDI enterprises (2,023 cases, 73.8%). Those occurred in private ones were 631 cases, accounting for 23%.

# **Part 4**

## **Some policy recommendations**

# Some policy recommendations...

- Policy makers should change their mindset and the way they think when formulating policies to encourage investment and business development.
  - Observing market principles.
  - Reference to best international practices.
  - Avoiding interfering and intervention the business of enterprises.
  - Eliminate the approach that the government will provide direct assistance or deliver support programmes. Other institutions such as business associations, services providers, centers, companies to assist enterprises should be promoted to take over this role..
  - Observing the principles of the market, and that “enterprises can do whatever that is not prohibited by the law”

# Some policy recommendations...

- Do not abuse fiscal incentives.
- Incentive forms should be more innovative and be more suitable to the real demand of enterprises. It requires policy makers to “think harder” when formulating policies and support programs.
- Using tax incentives appropriately and comply with international practices: efficiency, fairness, simplicity and transparency.
- Support policies need to be focused, systematic and implemented in an integrated manner. Patchy and piecemeal support often do not work and do not make a difference for the recipient enterprises.



# Some policy recommendations...

- Domestic enterprises, especially private ones, need to be considered as the pillar of the economy in order to build an autonomous economy,
- A balance in attracting domestic and foreign investments should be established in investment encouragement policies.
- The cornerstone of the national industrial policies Policies and programs should be domestic enterprises, specifically private ones.
- Discriminatory incentives for SOEs and FDI enterprises and at the detriment of private enterprises should be removed.
- **For detailed recommendations and the whole policy recommendation matrix, please refer to the report.**

# Thank you!

The full report can be downloaded from  
<http://luatdoanhnghiep-dautu.com> and  
[www.economica.vn](http://www.economica.vn)