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► Defining legal status for household businesses in Viet Nam

Key to formalization



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for household businesses
in Viet Nam**

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Le Duy Binh

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► Abbreviations and Acronyms

CIEM	Central Institute for Economic Management
DDCI	District and Department Competitiveness Index
FDI	Foreign direct investment
GDP	Gross domestic product
GSO	General Statistics Office
ILO	International Labour Organization
LLC	Liability Limited Company
MPI	Ministry of Planning and Investment
OECD	Organisation for Economic Co-operation and Development
SME	Small and medium-sized enterprise
VCCI	Viet Nam Chamber of Commerce and Industry



► Executive summary

In Viet Nam, the individual business sector (comprising household businesses, business individuals and other forms of individual business entities) currently contributes about 30 per cent of gross domestic product (GDP) annually. The country has approximately five million household businesses according to the General Statistics Office (GSO, 2022). However, according to business registration offices at district people's committees and tax authorities, only 1.7 million are registered and fulfilling tax obligations – contributing about 1.6 per cent to the State budget. This leaves 3.3 million household businesses unregistered. This is a significant gap between active household businesses as counted by GSO and those registered with local authorities. The number of persons employed in the household business sector is 8.49 million (GSO, 2022).

In 2021, the average size of employment in the household business sector was 1.68 workers per household business, while the average capital was 181 million Vietnamese dong per household business. As demonstrated by the size of employment, capital, fixed assets and revenue, household businesses are mostly micro in size, individually-run in nature and with the household head the sole proprietor and worker. Household businesses share the same features and nature as business individuals, sole proprietorships, or traders (sole proprietorship) as commonly found in other countries.

Viet Nam's Civil Code previously recognized the legal status of household businesses and cooperative groups in parallel with the legal capacity of individual/natural persons (cá nhân) and legal entities (pháp nhân). However, according to Articles 101 and 104, the Civil Code 2015 passed by the National Assembly no longer recognizes the legal status of household businesses and cooperative groups. This is because this legal entity according to the legal definition of the Civil Code 2015 is understood as recognition by the State for an organization (group of people) that can exist, operate independently and be responsible before the law. If an organization has a legal person status, that organization has all the rights and obligations of a legal person as provided for by law. However, a household business is considered self-owned with unlimited liability for production and business activities, and does not have legal status according to prevailing Vietnamese laws. Moreover, a legal party to a contract must be a legal entity (a company or organization) or an individual (natural person). Hence, as a household business in the eyes of the law is neither a company nor an individual it cannot be a party in a legally binding contract.

The Civil Code only recognizes individual/natural persons (cá nhân) and legal persons (pháp nhân). Accordingly, the legal capacity of household businesses and cooperative groups is now defined as that of individuals and their relationships represent those between individuals. To summarize, within the current legal framework since 2015, household businesses are not recognized for commercial transactions and are neither legal persons nor legal entities. Thus, they are excluded from all competitive bidding.

In Viet Nam's current legal system, except for Decree No. 01/2021/ND-CP which provides regulations on household business registration, no legal document provides a definition of a "household business", including its legal status. Therefore, the legal status of household businesses is opaque, even when registered. This results in numerous challenges for household business, especially when it is incumbent upon them to determine their legal status as subject to the law in business transactions.

To address this challenge, a two-pronged approach has been adopted in recent years to define and improve the legal status of household businesses. Firstly, regulations provided stipulations on mandatory registration and incentive measures (after mandatory requirements proved unsuccessful and were dropped post 2015) to encourage household businesses to register as enterprises under the Enterprise Law. Secondly, efforts were made to bring household businesses under the Enterprise Law.

Both efforts were unsuccessful due to a failure to address the root causes of the problem: the criticality of reworking and reforming the legal foundation and regulations for sole proprietorship to provide household businesses and related individuals a clear, solid and well-founded legal framework that is relevant and synergized with their nature and characteristics. Previous efforts sought to force household businesses and business individuals to register under the existing legal framework that contains numerous provisions unsuitable with the nature and characteristics of household businesses.

Viet Nam has already introduced regulations on sole entrepreneurship applicable to business individuals, sole proprietorship or sole traders as regulated in the Enterprise Law. However, in the Enterprise Law, this form of enterprise is named “doanh nghiệp tư nhân” which is often translated as private enterprises. This term in both the Vietnamese and English versions of the Enterprise Law fails to reveal the connotation of sole proprietorship or sole trader.

However, despite the availability of such regulations on sole proprietorship applicable to business individuals, being recognized as a private enterprise (sole proprietorship in nature) has become obsolete and no longer a suitable and low-cost option for individuals when starting a business. Instead, they either conduct business without registration or register themselves as household businesses. Between 2011–21, as many as 940,000 household businesses were formed compared to only 43,800 private enterprises (sole proprietorships) in the same period (MPI, 2023).

In 2022, only 1,344 (or 0.9 per cent) of 148,533 newly-established enterprises were registered as private enterprises (sole proprietorship) (MPI, 2023). This is a low number when compared with Singapore (20 per cent), Malaysia (61 per cent), the United States (73 per cent) and numerous European countries (80–90 per cent). This also explains why the number of active businesses per 1,000 population in Viet Nam is much lower than in other economies, and why it is not possible to achieve the target of 1.5 million active enterprises by 2025 set by the government.

The Enterprise Law has paved the way for the development of enterprises in Viet Nam, including private enterprises in earlier years of the law. However, recent revisions of the law have failed to keep pace with market developments. As a result, there remains a significant legal vacuum regarding the legal status of household businesses and other types of individually-run businesses. This is a paradox which needs to be addressed.

This paper sets out key limitations in current regulations applicable to private enterprises and expands on the various work-arounds that result in the continuing growth of household businesses that are not legally recognized. It proposes that efforts to reform and develop the household business sector should commence with reforming the legal framework and regulations on sole proprietorship, reforming stipulations and regulations related to private enterprises under the Enterprise Law.

As such, it is critically important to promulgate a law on sole proprietorship in the future. By developing a separate law on sole proprietorship and removing articles related to business individuals and private enterprises in the Enterprise Law, the regulations and legal framework applicable to business legal entities and business individuals can be separated, thus making regulations on enterprises in Viet Nam clearer, more systemic and transparent.

1 Detailed information is described in Part 3 of this report.

► 1. Introduction

Household businesses represent a unique feature of the Vietnamese economy. Before 1986, household businesses existed as small-scale commodity production units consisting of handicraft household-based and individual producers, farmers and small-scale service providers who did business with government permission. According to the General Statistics Office (GSO), as of 1975, these small-scale private production units accounted for 8.3 per cent of gross domestic product (GDP) (Statistical Yearbook 1983). In 1986, small-scale non-agricultural household businesses accounted for 23.2 per cent of total employment and generated 15.3 per cent of gross industrial output (Statistical Yearbook 1988).

After the Doi Moi (the Reform) policy was issued in 1986, household businesses flourished and became the business form preferred by millions of entrepreneurs and proprietors. Until now, starting a business in the form of a household business remains a widely popular option thanks to its simplicity, low cost and convenience. The household business sector has become an important pillar in Viet Nam's economy and plays an extremely important role in fostering economic resilience, especially in times of external shocks. Currently, about 8.49 million women and men are employed in the household business sector. The household, individual businesses and other forms of sole proprietorship contribute 30 per cent to GDP, but only 1.6 per cent to the annual State budget (General Department of Taxation, 2018).

Despite its important role, household businesses are classified as being in the informal sector as its legal status is unclear. Household businesses face numerous operational difficulties due to the ambiguity of its legal status.

The research is expected to contribute to the success of the scheme that should: (i) create a supportive, transparent, and equitable business environment for business households to establish, operate, and thrive to increase contributions to economic growth; (ii) reform the legal framework on supporting and developing household businesses to create conditions for business households to develop similarly to other economic units; and (iii) develop a policy to formalize household businesses through regulations on business registration and other regulations.

The specific objectives of this study are to:

- Identify issues with the business environment and challenges facing the establishment, registration, and growth of business households;
- determine the legal framework that will support and promote the household business sector, fostering an environment that will allow for development of business households on par with other economic units; and
- develop the legal status of business households and put forward policy recommendations to facilitate their formalization.

Methodology:

The study was carried out using a combination of methods, including:

- Researched and reviewed secondary literature, available data sources, including official sources from the GSO and other government agencies, and previous studies and research on household businesses, focusing on formalization.
- Conducted in-depth interviews with stakeholders and subjects related to the research issue. In-depth interviews aimed to consult and collect opinions and information from ministries, branches, and localities on managing, supporting, and developing household businesses under management of the sector.
- Proposed policies to improve the legal framework, promote formalization of household businesses, and encourage household businesses to register officially, thereby facilitating formalization and improving work conditions of employees in these enterprises.
- Conducted a rapid survey covering: (i) business households not converted into enterprises, advantages and disadvantages when operating in the form of business households, current situation of accessing capital, labour and science and technology; and (ii) business households converted into an enterprise and the conditions (including support policies and measures) to facilitate the decision to transform into an enterprise, advantages and disadvantages when operating in the form of an enterprise compared to a household business.
- Implemented in-depth interviews and surveys to support development of regulations and policies aiming to support the development of household businesses in the economy.

► 2. Past and current situation of household businesses in Viet Nam

2.1. Evolution of household businesses in legal documents

The term "household business" has been officially used in Vietnamese legal documents since 2006. They were formerly called by different names such as small-scale commodity production units, household-based businesses, small-scale industrial households, and individual household businesses. The following describes their evolution over time.

- *Before Doi Moi (1986)*, household businesses existed as small-scale commodity production units. They consisted of handicraft household-based and individually-run producers, farmers, and small-scale service providers who were allowed to do business with government permission.
- *After 1986 (Doi Moi) and following the issuance of the Law on Private Enterprises and the Law on Companies (1990)*, household businesses started to grow thanks to policies to develop a multi-sector economy. Before the Law on Private Enterprises and the Law on Companies (1990), household-based businesses and small-scale industrial households were officially recognized by Decree No. 27-HDBT by the Council of Ministers (now the government). During this period and under historical and socio-economic conditions, the development of household-based businesses and small-scale industrial households was slow due to a wide range of prohibited or conditional business lines as prescribed by law. According to the GSO, in 1989 the country had 333,337 registered household-based businesses and small-scale industrial households.
- *Following the issuance of the Law on Private Enterprises and Law on Companies in 1990 and before the Enterprise Law 1999*, household businesses existed as individually-run businesses (operated by an individual or group of individuals with capital below a threshold) in accordance with Decree No. 66/2000/ND-CP.
- *Between the issuance of the Enterprise Law in 1999 and Enterprise Law 2005*, household businesses existed as individual household businesses owned by an individual or household according to Decree No. 02/2000/ND-CP. As stated in Article 24, Decree No. 109/2004/ND-CP: "individual household businesses may hire no more than 10 employees. Individual household businesses that employ more than 10 employees or operate in more than one business location must be registered as enterprises".

- *Between the Enterprise Law 2015 and the Enterprise Law 2020*, decrees guiding the implementation of the Enterprise Law 2005² and Enterprise Law 2014³ renamed individual household business as “household businesses”. The legal regulations in this period added a provision that allowed a household business to be owned and run by a group of individuals (besides by individuals and sole proprietors). Since 2020, laws and regulations no longer limit the number of workers who can be employed by a household business.
- In the current legal system, except for Decree No. 01/2021/ND-CP (see Box 1) which only provides regulations on the registration of household businesses, there is no legal document that provides a definition of household businesses, including their legal status.

► **Box 1: Article 79, Decree No. 01/2021/ND-CP on business registration:**

“1. A household business is established by an individual or family household members who shall take full responsibility of the household business wholly by all of their property. If a household business is established by members of a household, one of them shall be authorized to act as the representative of the household business. An individual applying for registration of a household business or the person authorized by other household members to act as the representative of the household business shall be the owner of the household business.

2. Households engaged in agriculture, forestry, aquaculture and salt production, street vending, petty trade, consignment trading, mobile businesses and service provision that generate low income under a given threshold are not required to register as a household businesses, except for cases when they operate in conditional business lines. Provincial People’s Committees shall define the low-income thresholds applicable in their respective provinces.”

2.2. Current situation of household businesses

2.2.1. Number of household businesses

According to the GSO, the country counted 333,337 (registered) household-based businesses and small-scale industrial households in 1989. This number rose to five million household businesses by the end of 2021 (Table 1). The number of household businesses increased gradually over the years between 2011–19, then decreased slightly in 2020 and 2021. The annual growth in the number of household businesses between 2016–20 was 1.4 per cent, compared with 3 per cent during 2011–16. The growth slowed down and even decreased in 2020–21, mainly due to the negative impacts of the COVID-19 pandemic.

2 Decree No. 88/2006/ND-CP in 2006, Decree No. 43/2010/ND-CP in 2010.

3 Decree No. 78/2015/ND-CP in 2015.

► **Table 1. Distribution of household businesses by sectors**

Year	2011	2015	2019	2020	2021
Total (1,000 households)	4 236.3	4 754.8	5 377.7	5 200.4	5 067.4
By sector					
Industry-construction (% in total)	22.4	18.8	17.9	16.7	17.3
Trade and services (% in total)	77.6	81.2	82.1	83.3	82.7

Source: General Statistics Office (2021).

About 80 per cent of household businesses are in the field of trade and services, with household businesses mainly focusing on wholesale and retail trade, and repair of motor vehicles and motorcycles (more than 45 per cent), and hospitality and catering services (more than 16 per cent). The proportion of household businesses in other service sectors is relatively low, standing at 0.2-0.3 per cent in finance, banking and insurance services, 0.3-0.4 per cent in professional, scientific and technical services and 0.2-0.3 per cent in education and training. These sectors require highly qualified and skilled workers, capital and good governance. In reality, however, it is difficult for household businesses to meet these requirements.

In 2021, the average incidence of household businesses was one household business per 19.5 in the population. In other words, for approximately every 19 citizens, there is one who starts a business and earns a living in the form of a household business.⁴ This illustrates the popularity of household business among the population.

2.2.2. Contribution to GDP and job creation

The sole proprietorship sector (comprising household businesses, business individuals and other sole proprietorship entities) currently contributes 30 per cent of annual GDP. In 2018, more than 1.7 million household businesses fulfilled tax obligations and contributed 1.6 per cent of the State budget (General Department of Taxation, 2018). The annual average tax paid by each household business was 2.7 million Vietnamese dong. Meanwhile, the annual average contribution to the State budget by each company registered under the Enterprise Law was 1.7 billion dong.

⁴ This is higher than the proportion of one enterprise per every 111 residents in 2021.

► **Figure 1. GDP contribution by economic sector**

Unit: %



Source: Statistical Yearbook, Economic Census, GSO (2021 and others).

Household businesses provided employment to about 8.49 million workers in 2021. Workers employed by household businesses in 2020 accounted for 37 per cent of the total workforce of the business sector (Table 2), higher than in private sector enterprises (36.9 per cent), FDI enterprises (21.8 per cent) and state-owned enterprises (4.3 per cent). Given the sharp increase in the number of household businesses in recent years and the significantly higher density of these businesses compared with other business categories, it is apparent that household businesses are playing an important role in job creation.

► **Table 2. Number of workers by economic sector**

Unit: thousand persons

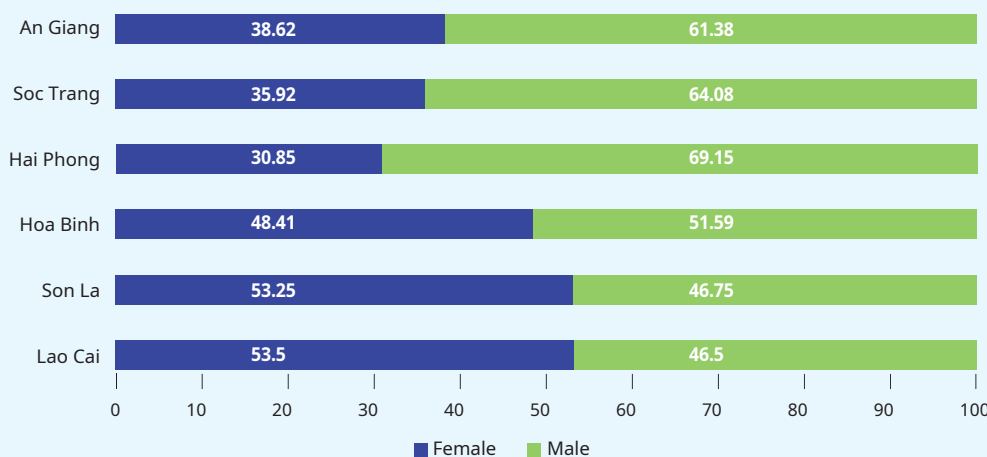
Year	Household businesses	State-owned enterprise sector	Private sector enterprises	FDI enterprises
2015	7 987	1 372	7 713	3 773
2018	8 668	1 127	8 977	4 714
2019	9 049	1 108	9 075	4 969
2020	8 656	1 005	8 607	5 090

Source: GSO (2021)

Household businesses also create employment for female workers, and are thus a means to drive women's economic empowerment. According to survey data for 2019–21 collected in 10 provinces by Economica Viet Nam, household businesses are creating more jobs for female workers. In all provinces covered by the survey, the percentage of women-led household businesses exceeded 30 per cent. In mountainous provinces, such as Hoa Binh, Lao Cai and Son La, the percentage of women who own household businesses approached or even exceeded 50 per cent. In addition, in surveyed provinces, female business owners also create more jobs for female employees when compared with male business owners.

► **Figure 2. Percentage of household business owners by gender**

Unit: %

Source: District and Department Competitiveness Index (DDCI) survey in some provinces, *Economica Viet Nam* (2021)

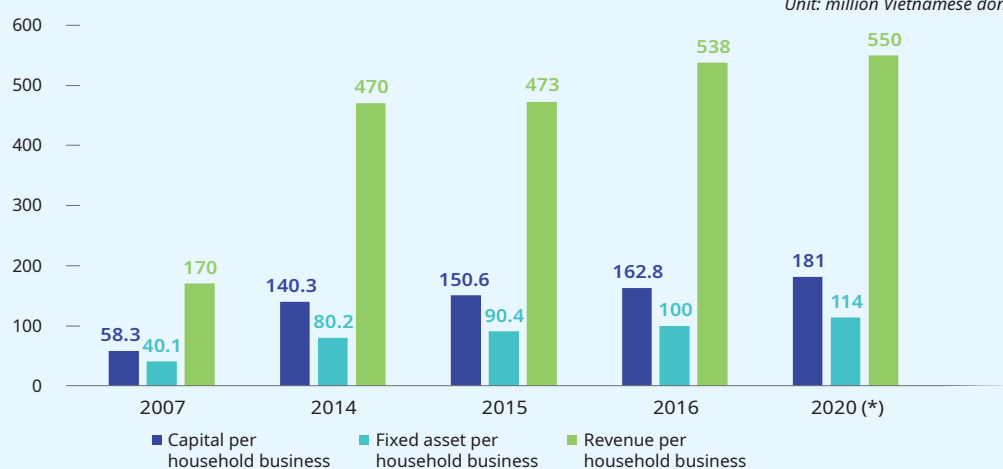
2.2.3. Operational characteristics of household businesses

The average employment size of a household business is low given the nature of individually-run businesses. On average, each household business had 1.8 workers in 2010, 1.68 workers in 2015 and stayed the same at 1.68 workers in 2021.⁵

Household businesses generally also have low capital size and fixed assets, reflecting the micro-scale operations of household businesses (Figure 3). In 2007, the average capital size of a household business was 58.3 million Vietnamese dong. This figure had climbed to 181 million dong by 2020. The average value of a household business's fixed assets was only VND114 million dong.

► **Figure 3. Size of capital, value of fixed assets and average revenue of a household business**

Unit: million Vietnamese dong



Note: *Preliminary and estimated.

Source: GSO, Statistical Yearbooks, *Economic Censuses* (2021 and other years)

Given their modest size of capital, the average annual earnings of a household business reached 473 million dong in 2015 and 550 million dong in 2020. As such, on a monthly basis in 2020, a household business generated about 45 million dong in revenue. With a profit margin of 10 per cent, this would translate to a monthly profit of 4.5-5 million dong per household business owners, including workers. This is much lower than the average monthly income of salaried workers (about 6.6 million dong in 2020).

The revenue landscape of household businesses is also diverse. According to the General Department of Taxation, about 110,000 household businesses generate more than 1 billion dong in annual revenue, or 100 million dong each per month. Out of five million household businesses, 1.7 million have obtained tax codes and paid tax. The remaining 3.3 million households have not obtained a tax code, partly due to poor compliance with requirements on tax code registration, but also because these household businesses generate less than 100 million dong in yearly revenue (under 8.3 million dong per month) and thus fall outside tax code registration.

Statistics on employment, capital, fixed assets and revenue of household businesses all underline that household businesses mostly operate at a micro-scale and individually-run basis. Most operate individually with household heads as the sole trader, sole proprietor and sole worker. Household businesses share the same features and nature as business individuals, individually-run businesses, sole proprietorship, sole trader as often found in other countries. This highlights the need for policy and legal reforms to take into account these features of household businesses as well as the household business sector's diversity to ensure policies and regulations governing the household business sector are relevant, practical and feasible. Given the information presented above, careful thought should be given to whether household businesses should be forced or encouraged to register as enterprises under current regulations of the Enterprise Law, or whether regulations should be reformed first before requiring household businesses to register under existing circumstances.

2.2.4. Why does the household business model prevail?

The household business model is a popular and simple way to start a business. Market entry procedures applicable to household businesses are not complicated and offer an opportunity for those with an entrepreneurial spirit to earn a living when not possessing much capital and experience. In addition, the model is suitable for underprivileged areas where other forms of businesses are not suitable. In fact, business households play an active role in preserving craft villages and national traditions, such as the accommodation and handicraft business model in Ha Giang, Hoa Binh Lao Cai and Son La provinces.

Household businesses are commonly the preferred form of business because:

- Regulations on conditions for establishment: All Vietnamese citizens, aged 18 years and above with full legal capacity and civil act capacity, are entitled to establish a household business. Those not permitted to set up enterprises like civil servants, public employees, officers, leaders and managers in state-owned enterprises can set up a household business. In other words, more subjects have the right to establish household businesses under law than various types of enterprises.

- Establishment procedure: The household business establishment procedure is simpler than setting up an enterprise under the Enterprise Law. Household business establishment dossiers include two main documents: (i) an application for household business registration and (ii) legal documents of individuals in case of household business-registered household members. Family-owned household businesses must supplement "a copy of the minutes of the household members' meeting on the establishment of the household business, a copy of a household member's written authorization for a member to own household business." Regarding the contents of establishment registration, a household business must only declare the following criterion: (i) household name, business address, (ii) lines of business, (iii) business capital and (iv) number of employees. The procedure and documents for establishing an enterprise are much more complicated.
- Place of business registration: Household business register their business in the respective district, to reduce travel costs. The agency competent to issue business household registration certificates is the Finance and Planning Department at district level, while the agency competent to issue an enterprise registration certificate is the provincial-level Business Registration Office.
- Business registration fee: The household business registration fee is equal to 50 per cent of the business establishment registration fee.

Thus, household business registration and the registration process offers many advantages. However, in terms of the scope of operation, business households face some limitations as follows:

- Scope of operation: Household businesses are no longer limited in the scope and scale of operation according to Decree No. 01/2021, but in reality they face limitations in comparison to registered enterprises, for example, in accessing bank loans and real estate. Also, they cannot access licenses for certain business. Households businesses also have less room to access large and international markets.
- Labour and social compliance: Household businesses often do not strictly comply with official regulations and regulations, especially those on production processes, quality of products and services, food hygiene standards, labour protection, safety and environmental protection. Often, they do not fully comply with regulations on accounting, auditing and tax payment, if in the form of securities.



► 3. Legal nature of household businesses

In Viet Nam's current legal system, except for Decree No. 01/2021/ND-CP which provides regulations on household business registration, there is no legal document with a definition of household businesses, including their legal status. Therefore, the legal status of household businesses is unclear, even if registered. This results in numerous difficulties and challenges for household business, especially when necessary to determine their legal status and be a subject of law in business transactions.

Viet Nam's Civil Code previously recognized the legal status of household businesses and cooperative groups in parallel with the legal capacity of individual/natural persons (cá nhân) and legal persons (pháp nhân). However, according to its Articles 101 and 104, the Civil Code 2015 passed by the National Assembly no longer recognizes the legal status of household businesses and cooperative groups. Accordingly, the legal capacity of household businesses and cooperative groups are now regarded as individuals and their relationships represent those between individuals.

The Enterprise Law neither defines nor provides provisions on household businesses. The law simply assigns "the government to develop regulations governing registration and operations of household businesses" (Clause 4, Article 217, Enterprise Law).

Household businesses are now governed by Decree No. 01/2021/ND-CP, which states they do not legally have their own assets. Rather, the assets of individuals and family members who own a household business are inseparable from those of the business. Household businesses do not have an official seal nor are they allowed to open representative offices and branches, but can expand their business activities by opening other business premises.

Sole proprietors, individuals and family members who own household businesses shall have unlimited liability for obligations under the business. This is similar to the unlimited liability of owners of private enterprises. In other words, if corporate assets are not sufficient to pay off debts, the business owner must use its own assets to repay the obligations incurred by the business. From this perspective, household businesses are similar to private enterprises specified in the Enterprise Law, or sole proprietorships or sole traders in many other countries.

This illustrates the fact that while mentioned in the Enterprise Law 1999, 2005, 2014, 2020, Commercial Law, Law on Tax Administration and some other legal documents, household businesses are yet to have their legal status clearly defined.

The prevailing laws and regulations, including the Enterprise Law and its implementation decrees, are silent on whether household businesses are individual/natural persons (cá nhân) or legal persons (pháp nhân). This is really the crux of the matter and means that future regulatory reforms related to household businesses should start with providing a clear-cut and decisive answer on how household businesses are legally defined.

Household businesses have different characteristics from those of joint-stock and limited liability companies, as shown in Table 3.

► **Table 3. Comparison between household and other types of business according to prevailing regulations**

Unit: thousand persons

	Types of business entities		
	Household businesses	Private enterprises	Limited liability and joint stock companies
Legal status	No	No	Yes
Liabilities of business owners, members and shareholders	Unlimited	Unlimited	Limited
Opening branches	No	Yes	Yes
Import and export activities	No	Yes	Yes
Bank loans under the name of the business	No	No	Yes
Raising capital by issuing securities	No	No	Yes
Purchase of shares in other companies	No	No	Yes
Registered at	At district level	At a provincial business registration office	At a provincial business registration office
Governed by Bankruptcy Law	No	Yes	Yes

Source: Based on Civil Code 2015, Enterprise Law 2020, Bankruptcy Law 2014, Circular No. 39/2016/TT-NHNN of the State Bank

According to its Articles 101 and 104, the Civil Code 2015 no longer recognizes the legal status of household businesses and cooperative groups. Instead, it only recognizes such capacity as individual/natural persons (cá nhân) and legal persons (pháp nhân).

On the basis of the Civil Code, regulations covering finance, credit, banking and contracts, among other areas, also no longer recognize the legal status of households as a party to civil contracts. Transactions with banks, credit institutions and financial companies are also deemed as relationships between these institutions with individuals who own household businesses rather than with the household businesses. Therefore, borrowing from banks in the name of the businesses is not possible. Instead, household businesses can take loans in the form of credit contracts between a

credit institution and the proprietor who owns the household business.⁶ Difficulties are also encountered when entering into civil contracts under the name of the household business.

Overall, tax regulations have been improved in line with principles articulated by the Civil Code. The Law on Tax Administration 2019 handles the status of household businesses in a relatively clear and straightforward manner. According to the law, the tax code granted to a household business is actually the tax code of the individual representing the household business. Thus, the Law on Tax Administration defines the legal capacity of household business as individuals. This has become a commonly accepted practice by the tax authority.

In essence, the legal changes in line with the latest Civil Code or regulations in the banking and tax sectors are appropriate from a legal development perspective and in line with international practices. These changes provide the initial basis for reforms in line with good regulatory practices, and in step with the nature of household businesses. Difficulties faced by household businesses in accessing bank credit, opening bank accounts, or entering into contracts can be attributed to that provisions on the definition of household businesses, their legal status and registration procedures that have failed to catch up with the principles articulated in Articles 101 and 104 of Civil Code 2015.

In fact, maintaining the legal capacity of household businesses today goes against the Civil Code and regulations in the banking and tax sectors. This issue needs to be addressed to optimize enabling conditions for development of the household business sector.

The approach adopted in recent years to define and improve the legal status of household businesses has taken two directions. Firstly, regulations provide stipulations on mandatory registration and incentive measures (after mandatory requirements proved unsuccessful and were dropped) to encourage household businesses to register as enterprises under the Enterprise Law. Secondly, efforts are made to bring household businesses under the umbrella of the Enterprise Law.

6 According to Circular No. 39/2016/TT-NHNN, stipulating lending transactions of credit institutions or foreign bank branches with customers, a customer performing a borrowing transaction with a credit institution refers to any legal entity or individual, including: (i) legal entities established and operated within the territory of Viet Nam and/or those established abroad and legally operated within the territory of Viet Nam and (ii) Vietnamese and/or foreign nationals. This means that household businesses and private enterprises are not permitted to borrow bank loans under the name of household businesses or private enterprises.



► 4. Recent initiatives to establish the legal status of household businesses

4.1. Converting household businesses into enterprises

Transforming household businesses into enterprises was first regulated in the Enterprise Law 1999. According to the law, *"the government should provide guidance and create favourable conditions for large-scale individual household businesses operating under Decree No. 66/HDBT dated March 2, 1992 of the Council of Ministers to be converted into enterprises, perform business registration and operate under the Enterprise Law"*. Then, the Enterprise Law 2005 clarifies further, that "household businesses that regularly employ 10 or more employees must register as enterprises in accordance with this law". The Enterprise Law 2014 retains this requirement. However, the Enterprise Law 2020 removed the stipulation.

The Law on Small and Medium Enterprises Support 2017 provides for incentives to small- and medium-sized enterprises (SMEs) which graduate from household businesses (Article 16). In addition, at the local level, there are mechanisms and policies to encourage household businesses to register formally as businesses, especially those that meet eligibility conditions prescribed by the Enterprise Law. Support may include exemptions from enterprise registration, stamp-making and licensing fees as well as cost of accounting software and business signboards. Despite these mandatory or supportive policies, the number of household businesses switching to formal enterprises under the Enterprise Law has been negligible.

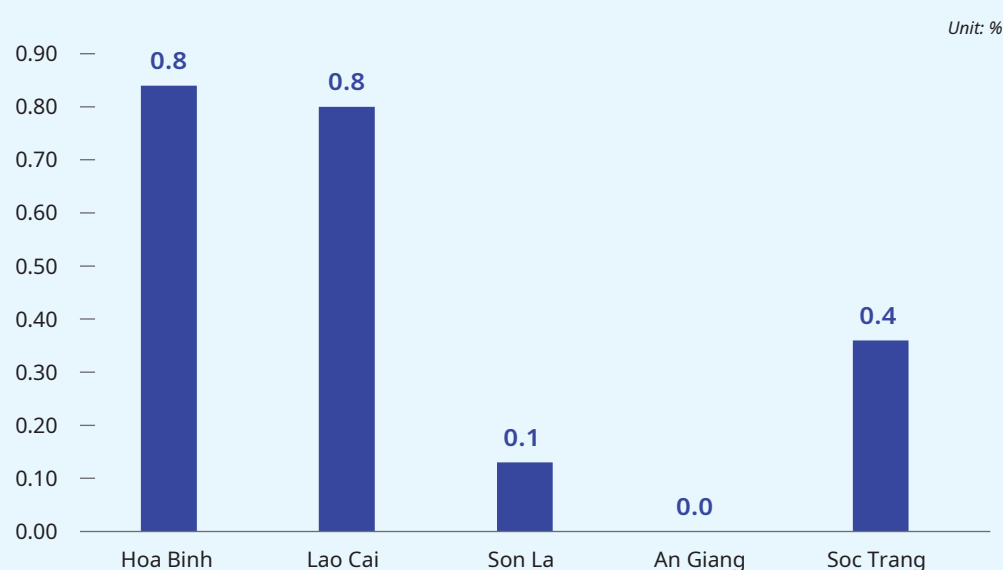
According to a survey of 374 household businesses and 46 enterprises by the Asian Development Bank (ADB) and the Central Institute for Economic Management (CIEM) in 2017, only 17.8 per cent of surveyed enterprises graduated from household businesses and up to 80 per cent of enterprises started from scratch. The survey results also revealed that up to 11.3 per cent of household businesses had 10 or more employees, but only 5.6 per cent planned to switch to other business types in accordance with the Enterprise Law (pre-2020). In terms of capital size, 13.2 per cent of household businesses with a turnover from 300 million Vietnamese dong to less than 1 billion dong planned to register under the Enterprise Law, while only 8.7 per cent of household businesses with a turnover from 1 billion dong to 5 billion dong said they would do so.

By industry and area of operations, 11.7 per cent of household businesses providing hospitality and catering services said they would register under the Enterprise Law. By gender, 9.2 per cent of male-headed household businesses intended to register as an enterprise, but only 3.5 per cent of female-headed ones planned to.

Between 2018 and 2020, despite incentives from the Law on Small and Medium Enterprises Support, only 1,875 household businesses were registered as enterprises. This included more than 1,000 enterprises in the provinces of Thanh Hoa in 2018 and 2019, 247 in Ben Tre, 40 in Thua Thien-Hue, 13 in Soc Trang, 12 in Binh Dinh, 11 in Ninh Thuan, 10 in Dak Nong, eight in Ca Mau, six in Phu Tho, six in Lam Dong and two in Phu Yen (Ministry of Planning and Investment, 2021).

In another study conducted by Economica Viet Nam in collaboration with provincial statistics offices within the framework of the District and Departmental Competitiveness Index (DDCI)⁷ survey, a question was asked on whether household businesses would convert into enterprises and operate under current Enterprise Law regulations. Only an extremely low percentage of household businesses responded “yes” to the question (Figure 4). Specifically, the percentage of individual household businesses reporting they would register or convert into enterprises under the Enterprise Law was only 0.8 per cent in Hoa Binh, 0.8 per cent in Lao Cai, and 0.4 per cent in Soc Trang. In An Giang, out of more than 1,000 surveyed household businesses, none intended to register or convert into enterprises under the Enterprise Law.

► **Figure 4. Percentage of household businesses indicating they would register or convert into enterprises under the Enterprise Law**



Source: District and Department Competitiveness Index surveys in Hoa Binh, Lao Cai, Son La, An Giang and Soc Trang provinces, Provincial Statistics Offices and Economica Viet Nam (2021, 2022)

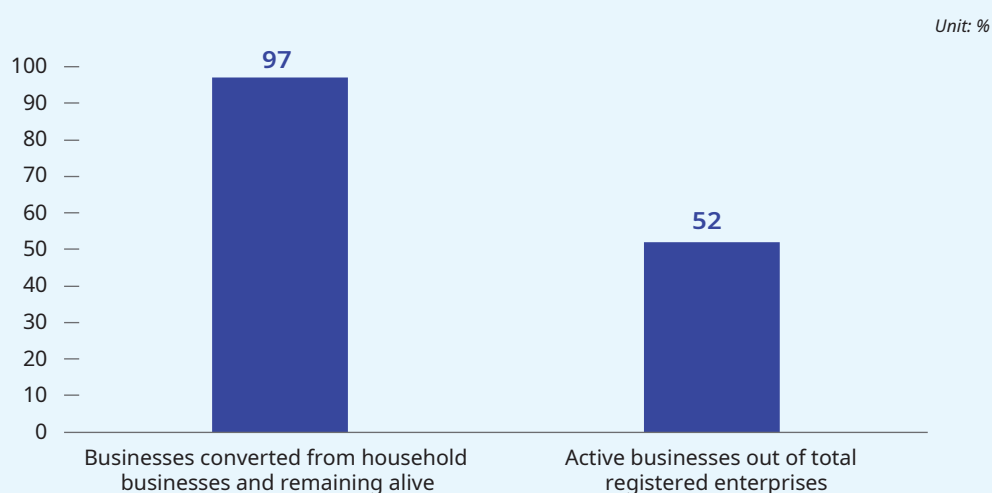
Between 2011 and 2021, about 1.15 million business ambitions were realized in the form of companies registered under the Enterprise Law, while nearly one million formed household businesses. Among the 1.15 million enterprises formed, only 578,000 enterprises or 50 per cent of registered enterprises remain alive and active. In contrast, nearly one million household businesses created during this period are still alive, as proven by the increased number of active companies and household businesses during this period.

⁷ See more at <https://ddci.org.vn/>

According to the MPI, in 2022 the proportion of enterprises graduating from household businesses and remaining active after five years was twice as high as the proportion of all enterprises registered under the Enterprise Law. After five years, as many as 97 per cent of businesses that graduated from household businesses remained active. This is favourable compared with the average survival rate of 52 per cent of all enterprises and companies registered under the Enterprise Law.

The robust vitality of household businesses and the fact they are the preferred choice of business start-ups should be considered carefully by policymakers when implementing business regulatory reforms.

► **Figure 5. Proportion of enterprises graduating from household business and remaining alive versus the proportion of the whole population of enterprises**



Source: MPI and Economica Viet Nam (2022)

According to the GSO, Viet Nam currently has about five million household businesses, with 1.7 million registered with a tax code. About one million household businesses were started between 2011-21 and remain active. Assuming that only half of these household businesses were registered as sole proprietorships or sole traders rather than as household businesses and given the high percentage (97 per cent) of enterprises which graduate from household business and remain alive as described above, Viet Nam would have had at least 500,000 formally registered enterprises. This would have brought the total number of active businesses much closer to the target of 1.5 million as articulated in Resolution No. 10-NQ/TW of the 12th Party Central Committee on private economic development.

4.2. Inclusion of household businesses as a type of business under the Enterprise Law

In 2020, the Enterprise Law was amended. The drafts of the amended law included regulations on converting household businesses into enterprises (Chapter VIIa of the final draft before discussions and approval). According to the draft, the Enterprise Law would recognize household businesses as a type of enterprise and outline the provisions for conversion of household businesses to enterprises. This provision in the draft was highly controversial, stirring heated debate on the topic, and disputed by numerous experts, government agencies, business associations, household businesses, sole proprietorships and National Assembly deputies.

Following a National Assembly Standing Committee request for votes from National Assembly deputies, 174/433 (40.2 per cent) of deputies agreed with having a chapter on household businesses in the (amended) Enterprise Law and 258/433 (59.58 per cent) endorsed the formulation of a separate law on household businesses.

Based on the majority opinion, the National Assembly Standing Committee decided to remove provisions in Chapter VIIa on household businesses and those on conversion of household businesses into enterprises. Also, to ensure continuity until a separate law on household businesses is promulgated, the government was tasked with providing guidance on registration and operation of household businesses.

The revised Enterprise Law was passed without the chapter and provisions on household businesses. This is considered by this report's author team to be a right decision by the National Assembly, especially in its vision for a separate law on household businesses. However, while this future law will govern and affect all currently active household businesses, it is recommended to scrap the proposed name, Law on Household Businesses. Rather, it should bear a different name such as the Law on Sole Proprietorship to better reflect the legal nature and characteristics of household businesses and for the law to cover other business individuals, individually-run businesses and other sole proprietorship entities. Household businesses would be just one of the subjects alongside with business individuals, individually-run businesses and other sole proprietorship entities governed by the law.

Also, several articles of the Enterprise Law need to be amended or annulled in parallel with or after such a separate law on sole proprietorship (or on household businesses) is formulated and promulgated. The following sections outline the rationale.

4.3. Practices for household businesses in other countries and lessons learnt from international experience.

It is worthwhile to look at how other countries, especially those with developed and mature markets and those with similar conditions to Viet Nam, have dealt with issues related to household businesses, and consider what lessons could be learned.

A first general finding from the review is that other countries do not have household businesses as conceived in Viet Nam, but rather rely on forms of sole proprietorship as a popular form for starting a business. In most countries, businesses fall in one of the three following categories: (i) sole proprietorship or sole trader, (ii) partnerships and (iii) liability limited companies/corporations. Based on these three categories, businesses can be divided into more specific sub-categories such as: (i) sole proprietorship, (ii) limited partnerships, (iii) single-member liability limited companies, two- or multi-member liability limited companies and (iv) joint-stock companies.

A business owned and run by an individual, where there is no legal separation between assets of that individual and its business, is called sole trader, sole tradership or sole proprietorship in Australia, the United Kingdom and United States – *entreprise unipersonnelle* in France and *einzelunternehmen* in Germany. The term ‘household businesses’ with the meaning and connotation as in Viet Nam cannot be found in any other country. Instead, sole proprietorship or sole trader as applied in other countries is considered the closest affiliation. This type of business is similar to household businesses as conceptualized in Viet Nam by sharing some key features: (i) the business is owned by an individual, proprietor, (ii) the registration is relatively simple, (iii) the owner is liable (unlimited liability) for all obligations under the business with all of its assets and (iv) profits from the business are accounted for as the proprietor's, owner's taxable personal income.

In terms of legal regulations, China enacted a separate law on business individuals and individually-run businesses. Named the Law on Sole Proprietorship Businesses, it came into force on 1 January 2020, consisting of six chapters and 48 articles. Among others, the law stipulates that a sole proprietorship business is owned by an individual who has unlimited liability for obligations related to the business. The proprietor can register the sole proprietorship with its home address as the business address, can sign employment contracts and shall pay employees' social insurance premiums. The tax applicable to sole proprietorship is personal income tax.

In Malaysia and Singapore, sole proprietorships or sole traders are governed by the Business Registration Act. In Thailand, sole proprietorships and individually-run businesses are governed by the Civil and Commercial Code. Regardless of the type of governing laws and regulations, sole proprietorships in these countries are the simplest, most convenient and cost-effective form for starting up and doing business. The regulations on registration, tax filings, financial reporting and other obligations are simple with low compliance costs. In these countries, tax applicable to sole proprietorship is personal income tax. As such, sole proprietorship and sole trader have become widely popular in different economies. For example in Southeast Asia, as of March 2023, Singapore had 575,527 businesses and companies. Among them, 144,234 (25 per cent) were sole proprietorships. In Malaysia, 554,900 out of 907,065 (or 61.2 per cent) of formally-registered businesses were sole proprietorships (SMECorp Malaysia, 2017).

In the European Union, among 2.3 million businesses registered in 2012, 1.6 million or 70 per cent were registered as sole proprietorships. This percentage was especially high in some countries, for example 92.3 per cent in France, 86.9 per cent in Poland, 86.4 per cent in the Netherlands, and 86.1 per cent in Czech Republic (EuroStat, 2013). In Hungary, among 450,733 active enterprises, 53 per cent were in the form of sole proprietorship (OECD, 2016). Some 73 per cent of small businesses in the United States were sole proprietorships (US Small Business Administration, 2013).

Lessons learnt from international experience

The review of international experience reveals that the term ‘household businesses’ with the meaning and connotation as in Viet Nam cannot be found in other countries reviewed. In these countries, business is based either on natural persons or legal persons. When deemed the natural person, work takes the form of sole proprietorship, sole trader or individually-run businesses. This form of business shares many similar characteristics with household businesses in Viet Nam.

The difference is that sole proprietorships in these countries, especially in developed economies such as the United States, Canada and Europe, are all registered formally. Due to its nature and size, sole proprietorship can be easily registered with the local government or online, with low compliance costs and simple accounting, financial reporting and tax filing regimes when compared with other types of business. Therefore, compliance costs and tax rates applicable to sole proprietorships in these countries are reasonable for business individuals and sole proprietors. This is the decisive factor of

attractiveness of this type of business, encouraging many entrepreneurs to start up in the form of sole proprietorship, as Vietnamese sole proprietors have been with the form of household businesses.

International good practices demonstrate the most important lessons learnt for Viet Nam in any reform of the regulatory framework for household business is to **consistently use sole proprietorship or sole trader as the legal form** for household business, and for individuals and proprietors if they wish to run their business on an individual basis. This principle should be used consistently in all laws and regulations related to household businesses. All other laws and regulations can be revised to treat household business as a sole proprietorship, just like international practices. This would create the foundation for regulatory reforms in business registration, tax management, accounting regimes, financial reporting, social insurance, bankruptcy and intellectual property rights protection, which are applicable to household business, business individuals and other individually-run businesses in Viet Nam.

Still, many questions might arise. For example, while sole proprietorships are popular in many countries as the simplest, most convenient and cost-effective form of doing business, why are they not growing in popularity in Viet Nam? The following sections will aim at finding answers to these questions.

► 5. Regulations on sole trader, sole proprietorship in Viet Nam

Viet Nam has already introduced regulations on sole entrepreneurship applicable to business individuals, sole proprietorships or sole traders as regulated in the Enterprise Law. However, in the Enterprise Law, this form of enterprise is named “doanh nghiệp tư nhân”, which is often translated as private enterprises. This term in both Vietnamese and English versions of the Enterprise Law fails to make the connotation of sole proprietorship or sole trader as applied in other countries.

Putting the terms aside, the definition of private enterprises in the Enterprise Law reflects the nature of sole proprietorship which can be applicable to business individuals, sole traders or individually-run businesses. According to the law, “a private enterprise is one owned by an individual who is wholly liable for the liability of the business by all of his/her assets” (Clause 1, Article 188, Enterprise Law). However, despite the availability of such regulations on sole proprietorship which can be applicable to business individuals, businesses in the nature of sole proprietorship as regulated in the Enterprise Law, private enterprises (sole proprietorship in nature) are becoming unattractive, obsolete and no longer considered by potential entrepreneurs as a suitable and low-cost option for business individuals to start a business. Instead, they either conduct business without registration or register themselves as household businesses as already discussed (see statistics in Sections 2.2.1 and 4.1). In so doing, they face numerous challenges due to their opaque legal status. This is in stark contrast to the fact that sole proprietorship is extremely popular in other economies as described earlier.

The lack of take up on the registration as private enterprises means the law does not meet the practical requirements of sole proprietors and entrepreneurs. The provisions on private enterprises in the Enterprise Law, although with significant impacts on the development of enterprises in the early stages, have become outdated and obsolete as the stipulations related to private enterprises were slow to be reformed.



► 6. Barriers to formalization of household businesses and causes

Previous initiatives to formalize household businesses, including conversion of household businesses into enterprises and inclusion of household businesses as a subject governed under the Enterprise Law, have been unsuccessful. This is largely because they failed to address the root causes of the problem, in other words the legal obstacles, constraints and limitations of regulations related to the type of private enterprise specified in the Enterprise Law.

In order to gain support from household businesses and business individuals, efforts to reform and develop the household business sector, including through formalization, should commence with reforming the legal framework and regulations on sole proprietorship, reforming stipulations and regulations related to private enterprises under the Enterprise Law. Section 2.2.4 has already outlined the reasons why household businesses have not formalized. This links to the following barriers identified as preventing formalization. Firstly, household businesses remain outside the currently defined “private enterprises” arena, which are entities provided incentives to register under the current law. Secondly, registration requirements for formal enterprises are considered too strenuous, including travel-time costs. Thirdly, because private enterprises are subject to known legal mandates, such as those that specify rules on the sale and lease of assets and bankruptcy, compliance is seen as too costly for household enterprises. Given the legal loopholes, they opt out.

The current Law on Tax Administration still has specific regulations on household businesses, including lump-sum tax (thuế khoán), but such regulations on accounting and tax reporting regimes applicable to household businesses are considered less strict. Registering or converting into private enterprises, sole proprietors or a household business owner will lose these significant benefits.

Moreover, given existing provisions in the Enterprise Law and other legal documents, the compliance costs for sole proprietorship under the private enterprise legal form is too high for business individuals and sole proprietors. This discourages them from registering and converting into private enterprises as stipulated in the Enterprise Law.

In addition, the private enterprise form has become even less attractive following regulations on single-member limited liability companies in the Enterprise Law 2005. As limited liability and single owner (member) entities, this model presents more advantages in this regard than private enterprises that makes the latter less appealing. A single-member limited liability company can also be owned by an individual but has the status as a legal entity and the owner only has limited liability

within its contributed capital. Before limited liability companies were legally recognized, private enterprises were preferred as they offered the possibility for a sole proprietor or sole entrepreneur to register. Private enterprises now lose this advantage to single-member limited liability companies, as owners of private enterprises have unlimited liability over their businesses' obligations. In addition, private enterprises do not have status as a legal entity.

Figure 6 shows the overwhelming dominance of single-member limited liability companies compared to private enterprises (both of which can be owned by one owner as stipulated in the Enterprise Law).



As seen in the figure, the single-member limited liability company model is much-preferred when starting a business. Out of 4,185 household businesses that converted into enterprises during 2018–22, 77 per cent became single-member limited liability companies and only 2 per cent chose to register as private enterprises.

► 7. Survey findings for household businesses and enterprises converted from household businesses

7.1. Survey of enterprises converted from household businesses

Methodology of the survey

In order to gain an understanding of the perception of enterprises that convert from household businesses and those that consider this option, the enumerators conducted a rapid survey of household businesses and enterprises converted from a household business.⁹

Despite the limited budget, the survey was implemented online with a few questions, but the sample of household businesses covered major cities across the country, including Ha Noi, Ho Chi Minh City, Da Nang and Can Tho. The sample was diverse in terms of registered capital (0 - 1 billion Vietnamese dong; 1 - 3 billion dong; 3 - 5 billion dong; and more than 5 billion dong). It also covered household businesses by years of operation (less than or equal to one year, one to three years, and more than three years), and by employment (0-10 workers, more than 10 workers).

The survey was implemented between late March and April 2023. As the survey was implemented online, the two enumerators mostly followed up with respondents by telephone and email. A total of 100 household businesses and enterprises were reached and 40 responded with qualified responses (questionnaires are available on request).

Data were processed by descriptive statistics methods, using Microsoft Excel. Data were tabulated and developed into graphs and charts to illustrate the responses to questions. The resulting sample details follow:

9 GSO, Statistical Yearbook, 2021.

► Table 4. Distribution of household businesses by sectors

Business information	Classification	Proportion
Address	Ho Chi Minh City	42.1%
	Ha Noi	36.8%
	Hai Phong	5.3%
	Can Tho	15.8%
Registered capital	Less than or equal to VND1 billion dong	57.9%
	1–3 billion dong	28.9%
	3–5 billion dong	7.9%
	More than 5 billion dong	5.3%
Years in operation under Enterprise Law	Less than or equal to one year	60.5%
	One to three years	31.6%
	More than three years	7.9%
Total number of workers	0–10 workers	86.8%
	More than 10 workers	13.2%

As seen in Table 4, most survey respondents were from Ho Chi Minh City and Ha Noi, accounting for 42.1 and 36.8 per cent of total respondents, respectively. Hai Phong had the lowest response rate with only two completed surveys, accounting for only 5.3 per cent.

Enterprises with registered capital from 0–1 billion dong accounted for the majority (57.9 per cent) of surveyed respondents, followed by 1–3 billion dong (28.9 per cent), 3–5 billion dong (7.9 per cent) and more than 5 billion dong (5.3 per cent).

Most surveyed enterprises converted from household businesses were in their initial years in operation under the Enterprise Law, with 60.5 per cent active for less than one year, 31.6 per cent in operation for one to three years and 7.9 per cent active for more than three years.

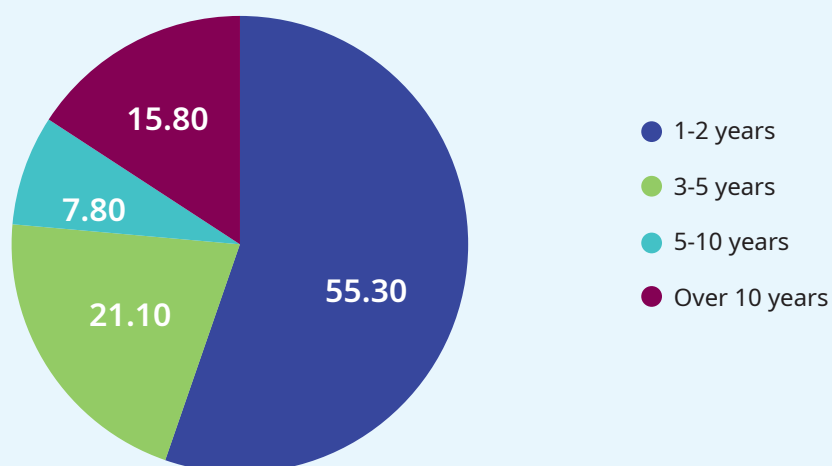
The vast majority of surveyed enterprises employed fewer than 10 workers (86.8 per cent), in contrast to those with more than 10 workers (13.2 per cent). The general conclusion is that surveyed enterprises converting from household businesses mostly have low registered capital and small employment sizes and were in their initial years of operation under the Enterprise Law.

Conversion into formal enterprises

According to the survey findings, 55.3 per cent of enterprises indicated they had operated as a household business for one to two years before registering as formal enterprises. In addition, 21.1, 7.9 and 15.8 per cent of enterprises had run their operations as household businesses for three to five years, five–10 years and more than 10 years, respectively. Most had decided to convert from household businesses to enterprises within a short period of time. Those operating as household businesses for a long time tended to go through a longer conversion process.

► **Figure 7: How long did you operate as a household business before formal registration as an enterprise under the Enterprise Law?**

Unit: %



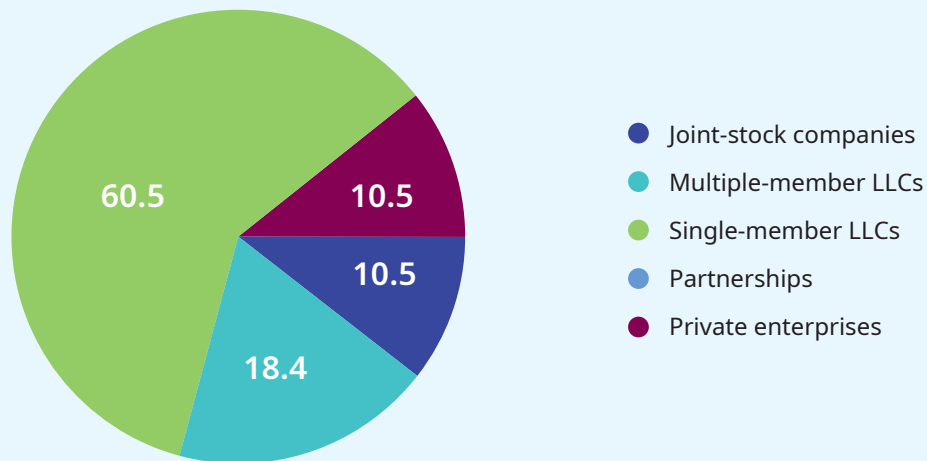
Before formal registration as enterprises, household businesses had delayed their conversion due to the following reasons: (1) no visible benefits and motivation for conversion (as indicated by 37.8 per cent of surveyed enterprises); (2) too many legal regulations and administrative procedures, coupled with complicated accounting regimes to be fulfilled by an enterprise (59.9 per cent); and (3) more tax payments and no longer eligible for selection of taxation methods as applied to household businesses (21.6 per cent).

For reasons of conversion into enterprises, 50 per cent of respondents said they wanted to establish a legal status to conduct transactions and develop at a higher level and larger scale, while 26.3 per cent were encouraged to do so thanks to available support policies from the local government and/or according to the Law on Small and Medium Enterprises Support. No surveyed enterprises converted from household businesses due to requests by local authorities.

For such a conversion, the majority (60.5 per cent) of surveyed respondents decided to register as a single-member limited liability company, with the remainder registering as other types of enterprises. The main reason for this choice, as indicated by surveyed enterprises, is the single-member limited liability company model is easy to manage and suitable with their scale of business, while also meeting business needs.

► **Figure 8: Which type of enterprises were mostly chosen for formal registration?**

Unit: %



When asked why they did not register as private enterprises, respondents stated they did not understand the nature and relevant regulations governing private enterprises (as indicated by 36.7 per cent of respondents), private enterprises did not have legal status but had unlimited liabilities (20 per cent) and they wished to maintain sole proprietors, but chose to be single-member limited liability companies to have a legal status and limited liability (30 per cent).

Among those registered as private enterprises, the majority (62.5 per cent) believed that private enterprises were sole-trader enterprises that shared similar ownership structures of household businesses, while 25 per cent indicated they did not carefully explore other forms of enterprises.

About half of surveyed enterprises believed that recognition of household businesses as a type of enterprise without other legal changes would not be meaningful to household businesses, while the rest perceived it as meaningful.

As suggestions to policymakers to encourage conversion of household businesses into enterprises under the Enterprise Law, the respondents advised to:

- Provide clear and easy-to-understand regulations on a type of enterprise in the Enterprise Law that reflects the nature of sole proprietorships (33.3 per cent).
- Revise regulations on tax, social insurance and health insurance that fits the nature of business individuals and sole trader enterprises (19.4 per cent).
- Reduce compliance costs for this new form of business, with similar exemptions currently provided to joint-stock and limited liability companies.
- Reduce taxes payable by business individuals to suit this business model and allow registration of business individuals and sole proprietorships under the Enterprise Law at a district level, similar to the current registration of household businesses (8.3 per cent).

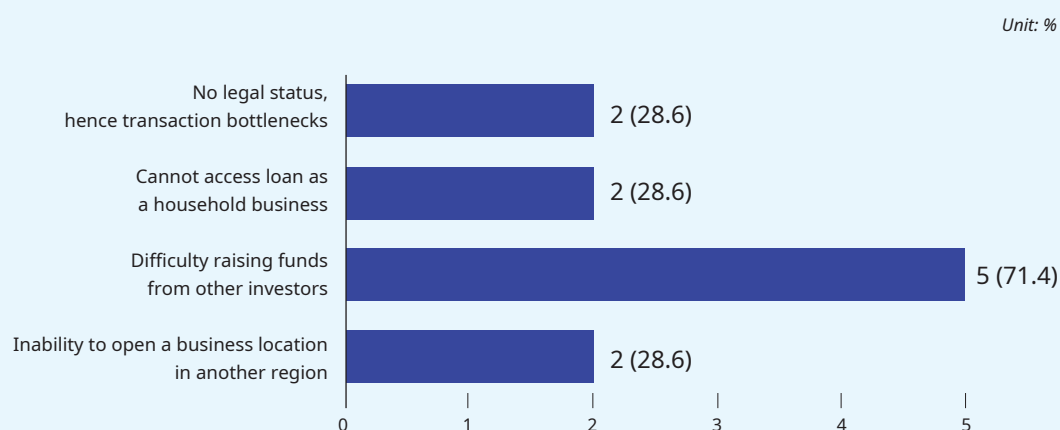
In the survey, the majority of enterprises (65.8 per cent) said they did not receive any support from the government related to their conversion under the Law on Small and Medium Enterprises Support. In regard to areas of support, only 31.6 per cent of surveyed enterprises indicated they received free consultancy and guidance from government support programmes on enterprise establishment applications and procedures, exemption from enterprise registration fees and charges for first-time provision of enterprise information, exemption from appraisal fees and charges for the first-time business licensing in conditional business lines and exemption from licensing fees for a period of three years from the date of first issuance of the Business Registration Certificate (54.5 per cent). Other aspects of support included exemption from and reduction of corporate income tax for a definite period in accordance with the Law on Corporate Income Tax (18.2 per cent) and free consultancy and guidance on tax administrative procedures and accounting regimes for a period of three years from the date of first issuance of the Business Registration Certificate (9.1 per cent).

7.2. Survey of household businesses

The survey of large-scale household businesses produced the following results:

- Most surveyed household businesses had capital of less than or equal to 500 million dong (66.7 per cent) and were in their initial one to two years of operations (44.4 per cent). All employed fewer than 10 people.
- The main difficulties encountered when running operations as household businesses included difficulties mobilizing capital from other investors (71.4 per cent), ineligibility for loans as a household business and absence of legal status, leading to challenges in transactions and preventing the formal registration to a different business location (28.6 per cent).

► **Figure 9: Key difficulties when running operations as household businesses**



- For household businesses planning for conversion into enterprises in the near future, the types of business entities most attractive were single-member limited liability companies (62.5 per cent) and private enterprises (50 per cent).
- Regarding willingness to convert into enterprises following proposed legal changes according to three listed options, most respondents indicated an unwillingness to convert their household businesses into enterprises according to all three options (66.7 per cent each). However, they believed option three to be most optimal to encourage household businesses to convert into enterprises (42.9 per cent).

- Regarding regulations that encourage and support conversion of household businesses into enterprises under the current Law on Small and Medium Enterprises Support, 77.8 per cent of surveyed household businesses indicated there were sufficient regulations to encourage such a conversion, while the remainder said current regulations were inadequate and further reforms were needed to reduce the burden of compliance costs and introduce regulations suitable for business individuals.

► 8. Legal reforms to establish the legal status of household businesses

Reforming legal regulations on sole proprietorship to support and develop the household and sole proprietorship sectors should be implemented in a structured, synchronous and systematic manner underpinned by the principles of observing the nature of sole proprietorship, business individuals, and individually-run businesses. The following steps are recommended:

8.1. Develop a separate regulatory framework on sole proprietorship

Developing a separate regulatory framework for business individuals and business legal entity has been the approach taken by many countries, especially OECD member nations, East Asian economies such as Japan and the Republic of Korea, and ASEAN members. China developed its Law on Sole Proprietorship Businesses, which came into effect in January 2000.

Given that the prevailing Enterprise Law already regulates private enterprises (which are sole proprietorships in nature), the best-case scenario should be the law being revised by reforming regulations in the law which are related to private enterprises in order to create legal frameworks in the same law, with one for private enterprises which are sole proprietorship and the rest for other forms of business legal entities such as liabilities limited company, joint-stock companies, etc.

It should be noted that in 2020, the Enterprise Law went under amendment, with the drafts including regulations on converting household businesses into enterprises. According to the draft, the Enterprise Law would recognize household businesses as a type of enterprise and provide that household businesses would be converted into enterprises. The subsequent vote of National Assembly deputies resulted in the removal of the chapter on household businesses from the draft law of the Enterprise Law 2020, and agreement with the formulation of a separate law on household businesses. On 17 June 2020, the Enterprise Law was passed with an approval rate of 90.7 per cent by National Assembly deputies with the chapter and the stipulation on converting household businesses into enterprises removed (Article 199a of the final draft).

In line with this direction, it is necessary to promulgate a law on sole proprietorship in the immediate future.¹⁰ This law should be developed in a way that governs all types of sole proprietorship and sole

¹⁰ In case it is decided that this new law on sole proprietorship will not be developed, the Enterprise Law should be amended instead. In this case, it is necessary to amend all stipulations, articles related to the form of private enterprises in the Enterprise Law according to the recommendations and suggestions in this report so that private enterprises can truly reflect the nature of their business as sole proprietorships.

traders in Viet Nam – such as business individuals, individually-run businesses and household businesses – a critically important group. Therefore, such a law should be given a name to reflect its scope, for example, the Sole Proprietorship Law or the Law on Business Individuals, Sole Trader and Individually-Run Businesses. The name of such a law will not only cover household businesses, but also many other types of sole proprietors such as business individuals, internet-based shop owners, professionals, and own-account workers, including freelancers or artists. These sole proprietors and business individuals need clear, simple, convenient, and low-cost regulations to join the formal economic sector as the absence of such a legal framework is acute.

Such a law also needs to provide a clear regulation that household businesses are a sole proprietorship by nature, and that they are treated as natural persons and business individuals in line with the Civil Code. This is the basis for all other legal regulations in fields that have a consistent and uniform treatment towards household businesses.

The law will provide provisions on such matters as registration, governance, accounting, financial reporting, general principles of taxation and social insurance, other obligations and benefits appropriate to the nature of sole proprietorships.

Moreover, it is most ideal if this law also makes it clear that its provisions will replace those on private enterprises currently prescribed in the Enterprise Law. Regulations related to private enterprises currently stipulated in the Enterprise Law 2020 will automatically cease to be valid after this law takes effect. This option will ensure that sole proprietorship is not governed by two laws at the same time.

In the event this option is deemed unfeasible, as such a provision may be too impactful on the Enterprise Law or require it to be amended in parallel, this law may still be developed and promulgated while the provisions on private enterprises in the Enterprise Law will remain for future amendment.

In the long term, no matter if the option of the Enterprise Law being revised with reformed regulations on sole proprietorships or the option of a separate law on sole proprietorships is selected, the regulatory frameworks for business legal entities and for sole proprietorship should be separated as depicted as per the figure below.

► **Figure 10. Separate Regulatory Frameworks for Business Legal Entities and for Sole Proprietorships**



Source: Le Duy Binh et al. (2023)

In case there is a change of mind regarding any plan to formulate a separate law on sole proprietorship to target mostly household businesses as decided by the National Assembly, the development of a separate legal framework for sole proprietorship and individual business can be accomplished by amending the Enterprise Law as this is actually the best-case scenario given the current context of Vietnam. In this case, all provisions on private enterprises as in the current law should be reformed according to suggestions and recommendations proposed in this report. In particular, the revisions should be firmly based on the principle of creating a separate regulatory framework for business legal persons and business individuals.

8.2. Measures applicable to private enterprises, household businesses, and other types of business individuals and sole proprietors after the new legal framework is introduced.

If a sole proprietorship law is developed and provisions on private enterprises in the Enterprise Law are removed, as in one of the scenarios described above, private enterprises registered under the Enterprise Law before the effective date of the new law will be automatically governed by this new law and treated as a sole proprietorship. If they do not wish to be treated as a sole proprietorship, they can choose to re-register as limited liability or joint-stock companies under the Enterprise Law.

If a sole proprietorship law is developed, while the provisions in the Enterprise Law are retained as currently, the private enterprise legal form will remain the same until relevant provisions related to them in the Enterprise Law are revised. Sole proprietors considering registration as household businesses will register under the new sole proprietorship law. After registration, they will be called sole proprietorships or sole trader enterprises. Business individuals (who engage in retail, services, professional activities or internet entrepreneurs) will register their business under the new sole proprietorship law.

Registered household businesses which already have a tax code (approximately 1.7 million) will be automatically governed by the new law and treated as sole proprietorships. Though they would be encouraged to register under the new law, this would not be mandatory. However, they would need to if applying for renewal or changes to their business registration certificates. For re-registration or new registration under the new law, business registration certificates will no longer name them household businesses, but sole proprietorship.

About 110,000 large-scale household businesses, with a turnover of more than 1 billion dong per year, that employ numerous workers and operate in many business locations can choose to register and run their business under this new law or consider converting their business into a limited or joint-stock company under the Enterprise Law.

The law will require that all business individuals, household businesses and individually-run businesses register under the new law, but it will also set a threshold on revenue or income below which the registered sole proprietorship, business individuals, household businesses and individually-run businesses are not subject to tax obligations, accounting and reporting requirements. A functioning database of household businesses, business individual and individually-run businesses can be used to access government support when needed as was the case during the COVID-19 pandemic or for government-targeted support for groups of household business and business individuals. Under current regulations,¹¹ household businesses and business individuals with revenue from production and business activities in a calendar year of 100 million dong or less are not required to pay VAT and income tax. However, they are still required to declare

¹¹ Circular No. 40/2021/TT-BTC providing guidance on value added tax, personal income tax and tax management of household businesses and business individuals.

and submit tax returns on time and take responsibility for the accuracy, truthfulness, and completeness of tax returns. Currently, there are 3.3 million household businesses nationwide in this category. These household businesses have yet to register with tax authorities.

8.3. Setting up a database on sole proprietors, business individuals and household businesses

The database of sole proprietorship, business individuals and individually-run businesses should be built and managed centrally together with the national enterprise database to form part of the National Enterprise Information System and the National Business Registration Portal. However, reforms to establish the legal status of household businesses must be carried out first, preceding other measures such as building a database and re-engineering the registration process for sole proprietorship, business individuals, individually-run and household businesses. This will ensure reforms and development of such a database and processes are systematic, clear, consistent and effective.

The law should clearly stipulate that business individuals, individually-run businesses and all other kinds of sole proprietorship shall be registered at the district level, rather than at a provincial business registration office, the same administrative level where household businesses are registered.

The registration of sole proprietorships, business individuals, individually-run businesses and household businesses can be conducted online via the National Business Registration Portal. Regarding the National Business Registration Portal, the management and delivery of business registration services for sole proprietorship, business individuals, individually-run and household businesses should be delegated and decentralized to 710 districts across the country, thereby reducing travel times and business registration costs borne by sole proprietors or household business owners when they choose to register their business as a sole proprietorship.¹²

Before a new law on sole proprietorship is promulgated, as proposed above, the government should issue a decree to govern not only household businesses, but also business individuals and sole proprietors so they are treated as sole proprietorships and sole traders in the future. The database on household businesses will need to be broadened accordingly.

8.4. Reforming regulations on governance, reducing compliance costs, protecting rights and legal status of sole proprietorship.

On the basis of principles established in Articles 101 and 104 of the Civil Code on legal entities and individuals, regulations applicable to sole proprietorship in terms of tax, labour, social insurance, finance, banking, credit, market entry conditions, intellectual property, bankruptcy and other legal provisions should also be revised towards a common, clear, coherent and consistent approach in line with international practices. Regulations on tax obligations and contributions to social insurance applicable to sole proprietorship will also need to be revised to become suitable to the individually-run nature of this kind of business.

¹² In addition, with this decentralization and the ability to register at district level for this form of "sole proprietorship" or "sole traders", sole proprietors are able to go to the same location, meet the same officer handling the documents, carry out the same process, receive the same documents as prescribed, and be granted a business registration certificate in a convenient and efficient way. Business registration facilitators at district level can also advise household businesses on the benefits of household business registration in the form of "sole proprietorship" or "sole traders" (private enterprise as currently stipulated in the Enterprise Law), rather than in the form of household business.

The current Law on Tax Administration still has specific regulations on household businesses, including a provision on lump-sum taxation. For alignment with the Civil Code 2015, the Law on Tax Administration 2019 stipulated that the tax code granted to household businesses is the tax code of individuals or representatives of household businesses. Thus, the Law on Tax Administration has defined the legal capacity of household business as individuals. This approach needs to be maintained for household businesses and all business in the form sole proprietorship under the future law on sole proprietorship.

The tax regime applicable to business individuals, individually-run businesses and sole proprietorship in this law should be personal income tax, reflecting the true nature of sole proprietorship.

Accounting standards, accounting reports and tax filing reports applicable to sole proprietorship, including business individuals and individually-run businesses as specified in this law should be developed in line with the nature of sole proprietorship and their legal capacity as individuals. Regulations on accounting standards, accounting reports, and tax reports applicable to these subjects must be different and simpler than those currently applied to private enterprises, limited liability companies and joint-stock companies covered by the Enterprise Law. Tax administration regulations also apply personal income tax deductibles for sole proprietorship, thereby enabling and encouraging people to start or register a business under this new law.

For household businesses not converted after the law on sole proprietorship comes into effect, it is necessary to consider a roadmap to phase out lump-sum tax policy and switch to personal income tax applicable to household businesses to ensure fairness and transparency with business individuals and sole proprietorships taking the initiative to register or convert under the new law. This will also encourage household businesses to re-register under the new law to access better legal rights and protections, now with a clearer legal status, in a level and transparent playing field, especially when such benefits as lump-sum taxes would no longer exist.

Regulations on contracts, bank account opening, intellectual property protection, import and export activities also need to be amended to make it more convenient and ensure protections for sole proprietorships, including business individuals and individually-run businesses.

The new law should also not apply the same strict requirements on office addresses of sole proprietorships, including business individuals and individually-run businesses, as applied to other forms of businesses regulated under the Enterprise Law. In fact, household businesses and all sole proprietors should be able to use their home address as registered business addresses. The law also should allow for the use of a lawyer's office or co-working space as a registered business address. This also reflects the nature of business individuals, contributing to reducing business costs, and in line with current trends of online business and virtual offices in the context of rapid development of the digital economy and industry 4.0.

8.5. Reforming regulations on labor and social insurance

Current regulations on labour relations and contracts as well as enrollment in social, health and unemployment insurance need to be clarified and supplemented to reflect the relationship between employees and sole proprietor (business individuals, owners of sole proprietorship and individually-run businesses). These regulations should be developed in a way that promotes harmonious industrial relations, while keeping compliance costs at a level appropriate to business individuals, owners of sole proprietorship and individually-run businesses.

The Law on Social Insurance needs to be amended to stipulate that “household business owners”, sole proprietorships (including business individuals, individually-run businesses) are subject to compulsory social insurance. In addition, compulsory social insurance products applicable to household business owners, sole proprietors (business individuals, owners of sole proprietorship and individually-run businesses), and employees working in these businesses must be improved to become more affordable and suitable with the nature of sole proprietorships with attractive contribution conditions and benefits.

Social insurance benefits and products for sole proprietorships (including business individuals, sole owner enterprises or sole trader enterprises) should always be based on the principle that these household businesses are business individuals rather than a business legal entity. Therefore, social insurance products and regulations must be sufficiently suitable and attractive to sole proprietors and business owners to ensure they enroll themselves and their employees.

8.6. Communication on the benefits and limitations of sole proprietorships

It is essential to conduct communication and awareness-raising activities to highlight the advantages of sole proprietorships. Indeed, sole proprietorships (including business individuals, individually-run businesses) need to be widely promoted as a simple, convenient, low-cost and officially recognized form of business, and a good alternative to household businesses. These communications activities must be realistic and supported by regulatory reforms to maintain the true advantages of this type of enterprise, as described above.

The communication should also help the public and entrepreneurs understand the disadvantages or limitations of sole proprietorships so they can make the best decision while choosing business legal entity form like liabilities limited, joint-stock companies or sole proprietorship when starting up or when deciding to graduate from sole proprietorship to business legal entity.

► 9. Conclusions

Establishing and defining the legal status for household businesses and other individually-run businesses through creating a clear and practical legal framework in line with international good practices, should be considered a key priority of law-making agencies and regulators. Such a legal framework will lay the foundation for reforms and sustainable development of household business, business individuals and individually-run businesses, which currently contribute up to 30 per cent of the country's GDP.

Changes to legal regulations on household businesses should also target business individuals, individually-run businesses and other sole proprietorship entities which are booming and increasingly common in Viet Nam. However, these businesses and individuals do not have a legal framework that provides a simple, low-cost, convenient, and natural vehicle to start their business in a formal way. Developing a separate law on sole proprietorships would help solve the problem related to legal status for not only household businesses, but also for other business individuals and other individually-run business entities operating in an increasingly high number within the economy.

As outlined in this report, a clearer and more effective legal status will be hugely advantageous for the development of the household business sector, business individuals, and other individually-run business entities operating in Viet Nam's economy. This will have a direct contribution to the key national goals of enterprise development, improving competitiveness of the economy and business sector, and expanding the formal sector and employment across the country. These reforms are, therefore, highly meaningful both in social and economic development terms.

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ILO Country Office for Viet Nam

-  Green One UN House
304 Kim Ma Street, Ba Dinh, Ha Noi
-  Email: hanoi@ilo.org
-  Tel: +84 24 38 500 100
-  www.ilo.org/hanoi
-  www.facebook.com/Vietnam.ILO
-  www.instagram.com/ilo.vietnam

