

**ECONOMIC GOVERNANCE AND DEVELOPMENT IN VIETNAM AND  
MOZAMBIQUE  
(‘FFU Project’)**

**Activity 7: Enterprise Development and the Private Sector**

**Reforms and Renovations of State-owned Enterprises in  
Vietnam**

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## **Abbreviation**

BG	Business Group
EVN	Electricity of Vietnam
FIE	Foreign-invested enterprises
GSO	General Statistics Office
HOSE	Ho Chi Minh Stock Exchange
NPT	National Power Transmission Corporation
SC	State Corporation
SCB	State Commercial Bank
SCERD	Steering Committee for Enterprise Renovation and Development
SCIC	State Capital Investment Corporation
SOE	State-owned enterprise
TKV	the Vietnam National Coal and Mineral Industries Group
VNPT	Viet Nam Post and Telecommunications Group
VPC	Vietnam Postal Corporation
VRG	Vietnam Rubber Group
WTO	World Trade Organization

## INTRODUCTION

State owned enterprise (SOE) reform and renovation are the focus of Vietnam's transformation process from a central planning economy to a market-based economy, which began in 1986. After 22 years, the SOE sector still maintains its leading role in the national economy. Thus the final aim of reforming SOEs is to improve the efficiency of resource usage and enhance business efficiency of this sector and then accelerate the growth and development of the whole economy.

*"Reforms and Renovations of State-owned Enterprises in Vietnam"* is a thematic research within Activity 7 - Enterprise Development and the Private Sector of the Denmark-funded Project on Economic Governance and Development in Vietnam and Mozambique. It aims at providing an overview of SOE reform and renovation process in Vietnam over the past 22 years.

The paper is structured into four sections. The second section describes the process of SOE reform and renovation during 1986 - 2008. The third section presents the results of SOE reform and renovation. Finally, the fourth section identifies challenges for future reforms and renovations of SOEs in Vietnam.

## **PART I. REFORMING AND RENOVATING SOEs DURING 1986- 2008**

### **1. Definition and classification of State-owned Enterprises**

#### ***Definition of State-owned Enterprise***

In Vietnam, the term “SOE” was first introduced in the Law on State-owned Enterprises 1995. Originally, an SOE was defined as “an economic organization invested, established and managed by the State, and engaging in business or public activities to attain socio-economic goals assigned by the State”. Subject to this definition were SOEs organized as independent enterprises, State corporations (SCs), or members of SCs, in which the State only exercised management rights over its invested capital.

The Law on State-owned Enterprises 2003 had clarified this definition by stipulating the share of State capital in the chartered capital of SOEs. Accordingly, an SOE is an economic organization in which the State owns all chartered capital or holds controlling proportion of capital contribution or share. The Law also classified SOEs into three types including State company<sup>2</sup>, shareholding company, and limited liability company), each of which has a different administrative model. State company and the “authorized representative” of the State’s contributing capital in SOEs were the two main subjects of adjustment in the Law on State-owned Enterprises 2003.

Changes made to the definition of SOE are part of the overall SOE reform in Vietnam, whose aim is to ensure the equality of enterprises before law, regardless of ownership. It can be seen later on that the Enterprise Law 2005 plays a key role in this reform, providing a common legal framework for the establishment, organization and operation of all enterprises, including SOEs.

#### ***Classification of SOEs***

By 2003, the classification of SOEs followed regulations in the Law on State-owned Enterprises 1995. Based mainly on types of business operation, the Law classified SOEs into two types:

- (i) SOEs conducting business activities mainly for profit purposes (for-profit SOEs).
- (ii) SOEs conducting public activities (not-for-profit SOEs), which are enterprises that produce public goods or provide public services in line with policies of the State or that directly carry out national defense and security tasks.

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<sup>2</sup> A state company is defined as an enterprise with 100 percent of state charter capital which is formed and managed and organized by the state according to the 2003 Law on SOEs. State company can be organized in form of an independent SOC or of a SC.

Of these two types, there are cases in which an SOE no longer has 100% of State chartered capital due to equitization. These cases fall in two categories: (1) SOEs in which the State holds the controlling share (from 50% and above); (2) SOEs in which the State holds special shares. Interestingly, these SOEs do not operate in compliance with the Enterprise Law but rather with the Law on State-owned Enterprises since issues relating to State ownership rights are regulated only in this Law.

The progress of SOE equitization, piloted since 1992, has led to changes in enterprises' ownership structure and thus outdated the Law on State-owned Enterprises 1995. The problems of ownership structure were resolved partly by the Law on State-owned Enterprises 2003, which classified SOEs into seven types, based mainly on the share of State-owned capital.

*The first type* includes all State companies. These are enterprises in which the State owns 100% chartered capital, and established, organized, managed, and registered under regulations of the Law on State-owned Enterprises 2003. State companies are organized in the form of independent State company or SC; the former shall not be included in the organization structure of any SC.

*The second type* includes State shareholding companies. These are shareholding companies whose shareholders are State companies or organizations authorized by the State to contribute capital, to be organized and to operate as stipulated in the Enterprise Law.

*The third type* includes one-member State limited liability companies. These are limited liability companies in which the State owns all chartered capital, organized, managed and registered under the stipulations of the Enterprise Law.

*The fourth type* includes State limited liability companies with more than one member. Members of these companies are either all State companies or some State companies along with other organizations authorized by the State to contribute capital, to be organized and to operate as stipulated in the Enterprise Law.

*The fifth type* includes enterprises in which the State holds the controlling share, equal or over 50% the chartered capital. The State has the controlling right over these enterprises.

*The sixth type* includes enterprises whose share of State capital contribution in chartered capital is below 50%.

*The seventh type* includes State companies having a controlling right over other enterprises. These are companies which keep the whole chartered capital or whose capital contribution or holding share accounted for more than 50% of the whole

chartered capital of other enterprises. The State holds a controlling right over these enterprises.

It can be seen that among the seven above-mentioned types of SOE, only State companies (the first type) operate in compliance with the Law on State-owned Enterprises; other types are classified in the Law on State-owned Enterprises, but include either shareholding companies or limited liability companies which operate in compliance with the Enterprise Law (only some aspects, especially the owner's rights regulated in the Law on State-owned Enterprises). This reflects the intricacy and discrepancy of regulations applied to SOEs. Besides, the Enterprise Law also set forth certain provisions specifically for SOEs, and stipulated the transformation of all State companies by 01 July 2010 into limited liability companies or shareholding companies in order to be applicable to this Law. Thus, next year will be a tough deadline that the SOE reform needs to meet.

## **2. Overview of SOE reform and renovation**

SOE reform and renovation are the focus of Vietnam's transformation process from a planned economy to a market-based economy, which began in 1986. After 22 years, the SOE sector still maintains its leading role in the national economy. Thus the final aim of reforming SOEs is to improve the efficiency of resource usage and enhance business efficiency of this sector and then accelerate the growth and development of the whole economy.

In Vietnam, the contents of SOE reform has been adjusted at different periods based on certain conditions. The reform itself was carried out step-by-step, following planned implementation process approved by authorized agencies. Basically, the main contents of reform include three points:

- (1) Reducing the number of SOEs while at the same time increasing their operation efficiency; making SOEs dynamic economic organizations, operating under laws and by market rules.
- (2) Separating the management function and State-owned representative in SOEs usually fulfilled by ministries, local governments and related government agencies.
- (3) Creating a fair competitive business environment for all kinds of enterprises, regardless of ownership.

For the past 22 years, SOE reform has been guided by these three points, but implemented in different ways. Prior to 1992, reducing the number of SOEs and separating enterprise finance from State budget were given top priorities. From 1992 to



1994, SOE reform had gone deeper through reorganization of the SOE sector, and through early formulation of a legal framework for the pilot equitization of SOEs. 1994 to 1997 was a period of establishing SCs and implementing the pilot equitization of SOEs. From 1998 to date many measures have been taken simultaneously and consistently to accelerate SOE reform, especially after the Enterprise Law took effect in 2006. The following table presents steps of SOE reform, as well as the planned implementation process.

**Table 1: Detailed steps of SOE reform and the planned implementation process**

1986-1990	1991-1993	1994-1997	1998-now	
			1998-2003	2004-now
Reduce direct subsidy from State budget to SOEs; Put the corporate finance system into action.				
Reduce the State's direct intervention in SOEs' business activities.	A legal framework for the operation of enterprises was formulated.	The Law on State-owned Enterprises 1995 was promulgated.	The Law on State-owned Enterprises 2003 was promulgated	The Enterprise Law was promulgated, making way to a uniform and consistent management system for all enterprises.
	Reorganize SOEs: - SOEs having a net profit must register, and apply for business license; - SOEs suffering net loss must be merged into those gaining profit or be dissolved. Pilot equitization commenced in 1992.	Establish large-scale SOEs titled State Corporation of 90-type or State Corporation of 91-type; Continue with SOE equitization and diversification.	Accelerate the equitization of State companies; From 1999: assign SOEs to the employees in the enterprises; lease, sell, contract out SOEs.	Equitize SCs; Pilot the establishment of State business groups (BGs)

*In the period 1986-90*

Reforms during the period 1986-90 included the removal of a subsidy system on price, salary, tax, for SOEs, while at the same time introducing business accounting into SOE sector to make it more independent. Even though many SOEs, especially those in processing, construction or commercial sectors, had been dissolved due to State subsidy cut, there still remained about 12,000 SOEs at the end of 1990. Nonetheless, the reform had its social consequence: the number of employees in SOEs took a nose-dive, from

12% of total labor force in 1986 to merely 6.9% of that in 1990<sup>3</sup>. Part of the employees who lost their jobs due to SOE restructure received early retirement compensation paid by the State budget. The rest, however, found it difficult to get a job in non-State sectors, especially with the serious lack of job support programs.

#### *In the period 1991-93*

From 1991 to 1993, SOEs had been divided into two groups based on their business performance. All SOEs gaining profit were required to register and have to apply their business license. The others were required either to be merged into enterprises with better business performance or dissolved. Thanks to this measure, the number of SOEs were halved, with around 3,500 being merged and nearly 2,500 being dissolved.

#### *In the period 1994-97*

Even after being merged, the majority of existing SOEs were still small-scale enterprises, which on average had under VND 1 billion of State invested capital per enterprise<sup>4</sup>. This led to the need of establishing the so-called large-scale State Corporations of 90-type and State Corporations of 91-type (hereinafter SCs) since 1994. SCs of 90-type were established and managed by ministries or provincial People's Committees; whereas, SCs of 91-type by the Central Government<sup>5</sup>. This process resulted in a huge impact. At the end of 1996, there were 17 SCs of 91-type operating in key economic sectors (electricity, steel, cement, oil and gas, posts and telecommunications) and 73 SCs of 90-type. Even though SCs made up only 24% of the total number of SOEs, they accounted for over 70% of total State capital, 56% of SOEs' labor force, and 77% of the State's tax revenues paid by SOEs. Thus, main proportion of State capital held by SCs and SCs created more jobs. The establishment of these Corporations is one of the main way of forming large capital-size SOEs with high competitiveness in producing and expanding domestic and international markets. However, even though the average capital size per SOE had in fact increased since 1996, the business efficiency of these enterprises had not much improvement. Until 2000, around one third of SOEs had suffered a net loss, 8.7% of which were members of SCs of 91-type and 13.2% of which were members of SCs of 90-type. Overdue debts of SOEs stacked to nearly 8% of GDP (at current 1999 price)<sup>6</sup>.

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<sup>3</sup> Nguyen Thi Tue Anh, 2003: Wachstumspolitik und Sozialpolitik in der Transformation zur Marktwirtschaft am Beispiel Vietnam.

<sup>4</sup> Nguyen Dinh Tai and Paul Hare, 1995: State Enterprise ownership transformation in Vietnam.

<sup>5</sup> SCs which were founded by the Prime Minister's Decision No. 90/TTg of March 7<sup>th</sup> 1994 were titled Corporations 90 and those which were founded by the Prime Minister's Decision No. 91/TTg of the same year were titled Corporations 91. Conditions to form Corporations 90 were that an SOE must have a legal capital of at least VND 100 billion (equivalent to USD 9.5 million based on 1994 exchange rate) and have at least 5 member SOEs. For a Corporation 91, the minimum legal capital is VND 1 trillion (equivalent to USD 90.5 million) and has at least 7 member SOEs.

<sup>6</sup> CIEM, 2002: Reforming SOEs: The Context of Vietnam and Experience from Other Countries.

Since 1995, SOE reform had gone deeper through various measures taken such as ownership diversification or transforming State companies to common types of company operating under the same legislations as for non-State enterprises. Up to date, these measures are still being implemented and will be assessed carefully in the rest of this paper.

### ***2.1. State-owned enterprise equitization***

In Vietnam, the term “equitization” is applied only to State companies and regulated in the Law on State-owned Enterprises 2003. In essence, equitization is the transformation of an enterprise owned solely by the State and operating in the legal form of a State company or one-member limited liability company into an enterprise owned by multiple holders operating under the legal form of a shareholding company stipulated in the Enterprise Law.

The goals of SOE equitization, despite undergoing several changes, are basically the four following points<sup>7</sup>:

- i. Transforming SOEs in which the State does not need to keep 100% chartered capital to enterprises owned by multiple holders, including the employees in the enterprises.
- ii. Mobilizing capital from domestic and foreign investors to enhance financial capability, innovate technology, and change the enterprise management.
- iii. Strengthening the real ownership of employees and shareholders; strengthening society’s monitoring over enterprise performance.
- iv. Balancing the interests of the State, enterprises, investors and employees in enterprises.

In terms of duration and equitization measures, the process of equitization can be divided into three periods: (1) pilot equitization period 1992-95; (2) accelerating period of equitization 1996-2005; and (3) State Corporation equitization period 2004 – now.

#### ***Pilot equitization period 1992 – 95***

The policy on SOE equitization was proposed in 1990, but commenced in 1992 through the pilot transformation of several SOEs into shareholding companies<sup>8</sup>; specifically, each centrally governed province/city would select one or two “volunteered” SOEs for pilot equitization. These selected SOEs had to be medium-scaled, and either had a net profit at the time or otherwise had at least a good business prospect. In addition, they could not be those enterprises the State needed to keep 100% chartered capital. A

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<sup>7</sup> Documents of the 10<sup>th</sup> National Party Congress of Vietnam

<sup>8</sup> Decision No. 202/CT of the Chairman of the Assembly of Ministers (now the Prime Minister) dated June 8<sup>th</sup> 1992 on the pilot equitization of volunteered SOEs

characteristic of this pilot transformation was that only staff and workers of these enterprises, domestic socio - economic organizations, and domestic individual investors were entitled to purchase shares.

From 1992 to 1993 a series of legal documents had been promulgated<sup>9</sup> to promote the progress of equitization. At the end of 1993, there were 23 SOEs in the pilot equitization list; yet only seven of them were selected to be transformed into shareholding companies<sup>10</sup>. In the next two years 1994 and 1995, the progress of equitization seemingly came to a halt while at the same time the number of SCs shot upward as previously mentioned. Thus, it could be seen that pilot equitization in this period was of little success. The main reasons for this were:

*First*, equitization was still a new and unfamiliar concept to management bodies, enterprises, and employees. Since they could not envision the impact of equitization on enterprise performance, equitization was considered highly risky by employees and enterprise managers who were used to work in the State-owned sector.

*Second*, the mode of implementing equitization was quite amateur, lacking transparency since there was basically no criteria or method to evaluate and appraise enterprise assets and land use value; it also could not be able to separate the source of assets which is formed by using State capital and which is enterprise assets. As a consequence, the process of equitization was prolonged and had a negative impact on employees and enterprise performance.

*Third*, local authorized bodies themselves were not enthusiastic about SOE equitization because SOEs had always been the main source of contribution to their provincial budget.

*Fourth*, the environment for equitization process had many limitations: stock market had not been established at the time; SOEs still received many priorities than non-State enterprises regarding to land usage, access to official credit source, social benefits for workers, and especially protectionist policies during this period; the business legal system had just been formulated and was under frequent adjustments, posing risks on enterprises after equitization. These limitations had hindered the progress of equitization, even just a pilot one.

#### *Accelerating equitization period 1996-2003*

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<sup>9</sup> Decision No. 203/CT of the Chairman of the Assembly of Ministers dated June 8<sup>th</sup> 1992 on making a list of selected SOEs for pilot equitization; the Prime Minister's Direction 84/TTg of March 4<sup>th</sup> 1993 on the acceleration of the progress of pilot SOE equitization and methods to diversify SOEs' ownership structure; Ministry of Finance's Circular No. 36/TC-CN dated May 7<sup>th</sup> 1993 on financial issues during the pilot equitization of SOEs.

<sup>10</sup> Nguyen Thi Tue Anh, 2003: Wachstumspolitik und Sozialpolitik in der Transformation zur Marktwirtschaft am Beispiel Vietnam.

Since 1996<sup>11</sup> the progress of equitization had been accelerated, after unsuccessful results of the previous pilot equitization. The targets and scope of equitization during this period were expanded to include all small- and medium-sized SOEs<sup>12</sup> those the State did not need to keep 100% chartered capital and with a so-called efficient business strategy. Yet after three years of implementation, the number of equitized enterprises only mounted slightly up to 32 in 1998. On average, there were 4.5 enterprises with small capital size being equitized each year during the period 1992-98 which was irrelevant to the 6,000 SOEs existing at the time.

The slow-down of Vietnam's economic growth after the 1997 Asian crisis had demonstrated inefficiencies of SOEs, including those of SCs of 90-type and 91-type; this made the acceleration of equitizing these SCs necessary, through restructuring<sup>13</sup> their members. Thus it can be seen that the targets of this equitization comprised not only independent SOEs, but also member companies of SCs. Besides, SOEs which had a net loss in two consecutive years would be dissolved.

To enhance the efficacy of equitization policies at SOEs' management bodies, in June 1998 the Central Steering Committee for SOE Management and Renovation was formed and in April 2002 changed its name to the Steering Committee for Enterprise Renovation and Development (SCERD). The function of this Committee was under direct control of the Prime Minister. Subcommittees were also founded at ministries, provinces, and SCs of 91-type. In addition, the circumstances for equitization was improved, for instance the establishment of Ho Chi Minh Stock Exchange (HOSE) in 2001. At the same time, a series of regulations on equitization, including equitized objectives, potential shareholders (including those who held right to buy shares at a discount price), maximum proportion owned by individual, methods of selling shares, methods of implementing equitization, and financial and labor solutions are promulgated and had taken effect as from 2002<sup>14</sup>. A notable change in the policy on equitization is that, since 1998 the foreign investors with permanent residency in Vietnam and overseas Vietnamese are allowed to be potential shareholders of equitized SOEs.

Despite many adjustments, at the end of 2002 there were only 700 SOEs fully equitized, much fewer than expected. Prior to being equitized, the majority of these SOEs were small-sized, accounting for merely 2% of total State capital in the SOE sector<sup>15</sup>. For so

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<sup>11</sup> The Government's Decree No. 28/CP of May 7th 1996 on transformation of SOEs into shareholding companies

<sup>12</sup> Excluding SOEs whose mode of equitization was to maintain current enterprise value, while issuing new shares as stipulated to mobilize more capital.

<sup>13</sup> Direction No. 20/CT –TTg on restructuring member enterprises of SCs, Decree No. 44/1998/ND-CP on transformation of SOEs and member enterprises of SCs into shareholding companies.

<sup>14</sup> These regulations were issued as attachments of Decree No. 64/2002/ND-CP on transformation of state companies into shareholding companies.

<sup>15</sup> CIEM, 2002: Reforming SOEs: the Context of Vietnam and International Experiences.

much effort that had been done to accelerate equitization, this was a disappointing result, and the main reasons were high risks of stock investment as well as the policy discrimination between SOEs and non-State enterprises.

*Period of equitizing State Corporations and large-scale State-owned enterprises 2004-now*

Prior to 2004, SOE equitization only targeted State companies and their dependent. However, according to the regulations of the Decree 187/2004/ND-CP, the equitization targets have been expanded to SCs, holding companies in BGs and in “parent-subsidiary company” groups<sup>16</sup> as well (see Table 2). Specifically, SCs (including State commercial banks and State financial organizations) as from 2004, and holding companies of any economic organization or “parent-subsidiary company” groups as from 2007 would be objectives of equitization. This expansion is necessary since the Law on State-owned Enterprises 2003 shall be expired on July 1<sup>st</sup> 2010. In addition, from the ten-year experience of equitization, the legal framework for the stock markets, investors’ rights protection, valuation of enterprises, and sale of shares in stock markets has been improved and become more transparent, thus helping to reduce the risks of equitization and to boost the confidence of investors as well as related parties after equitization.

A new point in equitization policy after 2004 is that foreign-invested enterprises (FIEs) are now permitted to buy shares in equitized SOEs. From 2007, foreign investors - both organizations and individuals – that engaged in investment activities in Vietnam have rights to own shares in equitized enterprises. Besides, the legal framework for investment and business activities has been remarkably improved since 2005, especially after the Enterprise Law and Investment Law came into effect. The essence of these two Laws is that they have established a common legal basis for all enterprises engaging in investment and business activities, regardless of ownership; and this basis is in line with WTO practices.

Besides the establishment of SCERD, the Government’s efforts to accelerate SOE reform in general and SOE equitization in particular could be seen in the establishment of the State Capital Investment Corporation (SCIC)<sup>17</sup> in June 2005. The aim of the establishment of the SCIC is to separate the function of administrative management and the authorized representative of State capital in enterprises after being transformed. SCIC functions as a representative of the State for the State capital in enterprises, and fulfils rights and obligations of the State as a shareholder in equitized enterprises. Until September 30<sup>th</sup> 2009, there have been more than 900 State shares in shareholding companies managed by the SCIC. At the end of 2008, the amount of State capital in

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<sup>16</sup> The legal basis for equitizing these enterprises can be found in Decree No. 187/2004/ND-CP of November 16<sup>th</sup> 2004 and Decree No. 109/2007/ND-CP of June 26<sup>th</sup> 2007.

<sup>17</sup> The Prime Minister’s Decision No. 151/2005/QĐ-TTg of June 20<sup>th</sup> 2005

equitized enterprises under SCIC's management has increased by 26%; chartered capital by 36%; enterprises' revenues by 44%; and enterprises' profits by 105%<sup>18</sup>.

Despite the Government's efforts, the pace of equitizing SCs and large-scale SOEs is still slower than expected. Equitized enterprises in which SCIC is the representative of State capital are mostly independent State companies. Moreover, the heavy work-load of managing and doing business with a huge amount of State capital allocated in many companies in different business sectors is likely to overwhelm SCIC's capability. Besides, due to its function as a shareholder, SCIC must understand thoroughly the specialties and areas of business activities of many enterprises, which is a formidable challenge for its members.

#### **Box 1: SCIC**

SCIC was founded on June 20 2005 and has started its functions officially since August 2006. SCIC was structured as an SC, having a Board of Management, a Control Board, a Board of Directors, and departments. SCIC functions in compliance with the Law on State-owned Enterprises and relating regulations. The Government exercises its ownership rights and obligations over SCIC. Chairman, Vice Chairman, and members of the Board of Management are appointed or dismissed by the Prime Minister. SCIC's head office is located in Hanoi and its branches in the South.

Of the 914 "representatives" who are in charge of managing State capital in equitized enterprises, 81% are enterprise managers, 16% are incumbent officials from ministries, branches, localities, and 3% are SCIC's officers<sup>19</sup>.

## ***2.2. Transferring, selling, contracting out, leasing State companies***

During the process of SOE equitization, it was deemed necessary to restructure small-scale SOEs having the following characteristics: the State did not need to hold them; they were not targets of equitization; their net loss was not too severe for them to be dissolved by law. These enterprises operated mostly in trading sector, small-scale production under district-level management. Modes of reforming these SOEs included transferring to their employees by signing a contract, or selling these enterprises to other organizations and individuals with the assurance of maintaining operation and jobs for employees. Based on different periods of equitization, targets of SOE transfer or sale were adjusted accordingly.

The first legal document on the sale and transfer of SOEs is the Government's Decree No. 103/1999/ND-CP on transferring, selling, contracting out, leasing SOEs

<sup>18</sup> Vietnam News Agency, posted on the OTC Stock Exchange website: <http://news.sanotc.com>.

<sup>19</sup> In reference of the Prime Minister's Decision No. 152/2005/QĐ-TTg of June 20<sup>th</sup> 2005, ratifying the organization and operation charter of SCIC, and the Saigon Economic Times on September 13<sup>th</sup> 2009.

promulgated in 1999. To date, this Decree has been amended and supplemented three times<sup>20</sup>, with Decree No. 109/2008/ND-CP dated October 10<sup>th</sup> 2008 being the most recent. Changes in the policy on transferring, selling, contracting out, leasing SOEs are presented in Table A.2 in the Annex, in which it can be seen that the capital size of objects of application has been adjusted upward and since 2008 companies with 100% State capital have been added to the objects of application. In addition, Decree No. 80/2005/ND-CP has expanded the buyers of SOEs to FIEs as well.

In fact, these modes of reforming SOEs (transferring, selling, contracting out, leasing) have received little success quantitatively. At the end of 1999 there were only 5 SOEs entirely sold. Till the end of 2002, the number of SOEs transferred to their employees for collective management stood modestly was only 41, and that of sold to the enterprise labor group was 32<sup>21</sup> - not to mention that most of these SOEs were just small-scale. Nonetheless, the positive impact of these methods is that they could maintain jobs and income for employees after changes in ownership; the State is also benefited as the efficiency of its capital usage.

### ***2.3. Transforming State companies into one-member limited liability companies***

The 2005 Enterprise Law stipulates that all SOEs subject to the Law on State-owned Enterprises 2003 are required to be transformed into limited liability companies or shareholding companies. Thus, after transformation even enterprises in which the State retained 100% chartered capital would be subject to the Enterprise Law. The suitable model of transformation for these enterprises was one-member limited liability company since they already had only one owner - the State.

SOEs in which the State retained 100% chartered capital mostly operated in areas of national defense and security, otherwise were those that play a key role in stabilizing macroeconomic and that provide public-utility goods and services. In order to retain 100% State capital in the chartered capital and for the Enterprise Law to be applicable, these SOEs have to be transformed into one-member limited liability companies<sup>22</sup>.

The transformation of enterprise type has been implemented since 2006 to restructure State companies, to introduce more efficient management models, the corporate governance into State companies, as well as to give more rights and responsibilities to

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<sup>20</sup> Decree No. 49/2002/ND-CP dated February 24<sup>th</sup> 2002; Decree No. 80/2005/ND-CP dated June 22<sup>nd</sup> 2005; Decree No. 109/2008/ND-CP dated October 10<sup>th</sup> 2008

<sup>21</sup> CIEM, 2002: Reforming SOEs: The Context of Vietnam and Experience from Other Countries.

<sup>22</sup> Decree No. 95/2006/ND-CP on transforming state companies into one-member limited liability companies, which replaced Decree No. 63/2001/ND-CP dated September 14<sup>th</sup> 2001 on transforming SOEs and enterprises of political, socio-political organizations into one-member limited liability companies and Decree No. 145/2005/ND-CP issued on November 21<sup>st</sup> 2005 by the Government, amending and supplementing several items of Decree No. 63/2001/ND-CP.



enterprise managers. Transformed enterprises play a more active role in making their business decisions. As they are now subject to the Enterprise Law, these enterprises are under the management and monitoring of only one authorized representative for State ownership.

#### ***2.4. Transforming State Corporations into the parent-subsidary company model and establishing State business groups***

Since 2004, SOE renovation has been accelerated through the transformation of SCs into the model of parent-subsidary companies<sup>23</sup>. The aim of this transformation is to improve business efficiency of SCs by changing the relationship between SCs and their member enterprises. Specifically, the old administrative, authority-based relationship between SCs and member enterprises was replaced with the new relationship based on common economic interests between SCs and member enterprises (through investment, technology, and market relationships). In the new model, SCs, being the parent companies, can control their member enterprises, being the subsidiary companies, through their role playing in capital, technology, and market fields. This relationship is based on the concept of mutual benefits for both SCs and member enterprises, and is compliant with Vietnamese law. In addition, every enterprise in this type of relationship has its own legal status and equals with each other by law. Besides, the parent-subsidary company model has also formed the basis for the establishment of BGs since the Enterprise Law took effect<sup>24</sup>.

Renovating SCs through their transformation into parent-subsidary companies and multi-ownership corporations with modern corporate governance system is expected to improve SOEs' competitiveness in domestic as well as international markets, at the same time trim down State monopoly, and end State subsidization for SOEs. Unfortunately, the pace of transforming SCs into parent-subsidary companies has been quite slow, contrasting with that of establishing BGs.

At the end of 2008 there were eight BGs established through the restructure of seven SCs of 91-type and the equitization of one SC of 90-type; the figure was expected to go up to ten in 2009<sup>25</sup>. The eight already-established BGs are pilot models resulted from

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<sup>23</sup> The Government issued Decree No. 153/2004/ND-CP on August 9th 2004 on the organization and management of state corporations, and on the transformation of state corporations and independent state companies after the parent-subsidary company model. This Decree was later replaced by the Government's Decree No. 111/2007/NĐ-CP dated June 26th 2007.

<sup>24</sup> The Law on Enterprises 2005 has only one stipulation about BGs under Article 149. Decree No. 139/2007/ND-CP by the Government guiding the implementation of Law on Enterprises contains one article stipulating some regulations on business group. However, the detailed regulations and guidance for BG formation and performance have not been promulgated. The Government is now drafting the Decree on formation, organization, performance and management of business groups.

<sup>25</sup> BGs resulted from the administrative decision of the Prime Minister include: EVN, VNPT, TKV, Vinatex, Petro Vietnam, Vinashin, VRG, Baoviet Holdings. The following BGs are expected to be incorporated in 2009: Vietnam Civil construction and Real estate group, which is under the management of the Ministry of Construction and formed on the basis of Song Da Corporation; and Vietnam

the administrative decisions made by the Prime Minister, and are under the Prime Minister's direct management. The structure of BGs comprises the headquarter and member companies, which function as parent and subsidiary companies, respectively. The fundamental difference between SCs and BGs is reflected through the relationship between SCs and their members and that between parent companies and subsidiaries in BGs. In the latter type, parent companies will control subsidiary companies, associated companies through the proportion of their invested capital in each subsidiary company and each associated company; technology capability; and market power (through signed business contracts between parent companies and subsidiary/associated companies). Moreover, in contrast to the case of SCs, parent companies shall not directly interfere in the operation of their subsidiaries, and every company – parent or subsidiary – shall have its independent legal status and be equal by law. Controlling right shall be done through parent companies' authorized representative in the Management Board, the Board of Members, or the Board of Directors in subsidiary enterprises.

### **3. Current situation of key policies for supporting SOE reforms**

#### ***3.1. Financial and capital management policies***

##### *State capital and property management*

In implementing the State Enterprise Law, the Government promulgated the Decree No.187/2004/ND-CP dated November 16<sup>th</sup>, 2004 on shifting the State corporate into the stock company, replacing the Decree No. 64/2002/ND-CP and Decree No.199/2004/ND-CP dated December 3<sup>rd</sup>, 2004 on the issuance of the regulation on the State corporate financial management and the State capital management at enterprises, replacing the regulation on the State enterprises' financial management which was issued in conjunction with the Decree No.59/CP and Decree No.27/1999/ND-CP and regulation on capital management at enterprises at the Decree No.73/2000/ND-CP.

These are the two among the documents on guiding the implementation of the 2003 State enterprise Law. The two Decrees has the key amendments and supplements aimed to strengthen and expand the reform process of State-owned enterprises and raise the effectiveness of SOEs. The amended contents focused on the following issues: expanding the equitization objects, simplifying the enterprise evaluation, the SOEs equitization process, strengthening the transparency and publicity in the equitization process, avoiding the closed equitization at enterprises, facilitating the investors, especially the strategic investors to hold the equity at equitized enterprises, linking the equitization to the stock market development. For the State corporate management, it has identified the ownership responsibility in capital investment in State company and

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Mechanical Industry and Assemble Group, which is under the management of the Ministry of Industry and Trade and formed on the basis of Lilama.

rights and responsibilities of the owners and enterprise executives, enhancing the responsibilities of the enterprise executives, in reporting to the owners, strengthening the supervision of the owners and self-supervision of the enterprises.

In order to implement the said two decrees, the Ministry of Finance issued the Circular No.126/2004/TT-BTC dated December 24<sup>th</sup>, 2004 providing guidelines on the Decree No.187/2004/ND-CP dated November 16<sup>th</sup>, 2004 on shifting the State corporate into the joint stock company, rapidly perfecting the documents on guiding the implementation of the Decree No.199/2004/ND-CP dated December 3<sup>rd</sup>, 2004 on the issuance of the financial regulation on State corporate and management of State capital invested in other enterprises.

The issuance of these under-law documents can be considered as a renovation of philosophy towards expanding the autonomy and strengthening the responsibility of SOEs; the mechanism of State capital management in SOEs has been improved. The development of the State Enterprise Law is clearer identification of responsibilities of institutions and individuals in managing and representing the State capital in enterprises.

The management State capital in equitized enterprises is executed by representative of State capital owner in accordance with State Enterprise Law in 2003 and stipulations in Regulation on financial management in SOEs and managing State capital in other enterprises, which was attached to Decree No. 09/2009/ND-CP dated February 5<sup>th</sup>, 2009 issued by the Government. The stipulations are as follows: (i) for shareholding enterprises transformed from member enterprises of General Corporations, parent companies and State-invested enterprises, these enterprises will continue executing the function of owner representative; (ii) for shareholding enterprises transformed from SOEs under direct control of Ministries and localities, the State Capital Investment Corporation (SCIC) will undertake the function of owner representative.

According to these stipulations, representatives of owners make decision on investment, contributing capital and adjusting investment capital in shareholding enterprises; appoint, displace, commend and reward, take discipline, decide salary, allowances, bonus and other preferential treatment for State capital owner representative; and assign tasks and direct the legal representative of State capital. The representatives will supervise and investigate the utilization of State capital and take responsibility for the efficiency, preserving and developing State capital in enterprises.

#### *Management of business revenue and costs*

The regulations on the scope of business revenue and costs are still incomplete and inconsistent. They are not relevant to practical situation of the market. There is still

misunderstanding in the function of State administration over enterprise and the function of State owners of SOEs.

### *Income distribution*

SOEs' income distribution mechanism has been changed in comparison to the previous one. It is reflected by proper recognition and evaluation of enterprises' autonomy in distributing after-tax profit.

Regarding wage policy, wage is included in the cost of goods sold and is compensated by revenue but due to low revenue of SOEs, the proportion of wage in revenue in these enterprises is still low. In fact, SOE workers do not live on wage but live on income. Their wage only accounts for 1/4 - 1/3 of their total income. As a result, wage is not an incentive for attracting workers and fostering business development.

For enterprise income tax, there is an inconsistency in terms of enterprise income tax between domestic investors and foreign counterparts, causing the inequality among investors.

The Government also has regulations on different types of compulsory funds within enterprises, causing difficulties for capital concentration.

Several shortcomings in financial management policies in SOEs can be seen as follows:

- Financial regulations are incomplete, insufficient and inconsistent;
- The State ownership over enterprises and property ownership of enterprises are not clearly defined;
- Although SOEs are more authorized in financial management, they still face many constraints and lack autonomy in operation.

### **3.2. Land policies**

Decree No. 187 stipulates that equitized companies will receive preferential treatment from the Government. In which, equitized companies are entitled to continue using social assets, such as nursery schools, clubs, these assets are not included in the enterprise value).

However, the identification of land value is one of constraints to the equitization because new Government's policies on land issue in equitization are not relevant to practices. Decree No. 109/2007/ND-CP dated June 26<sup>th</sup>, 2007 of the Government stipulating the transformation of 100 percent SOEs into shareholding enterprises requires enterprises in urban areas to calculate the value of land use rights (for land assigned) and value of geographical location (for land hired) into the value of enterprise. This requirement is difficult to implement because regulations stipulate that the market

value of land use rights needs to be evaluated in accordance with land use purpose in normal condition at the time of equitization and based on completed land transactions. It seems to be theoretically relevant and necessary but is impossible to implement in practice because of the following reasons:

- i. In reality, Vietnam's real State market always fluctuates depending on the Government's policies. Therefore, it is impossible to value the land use rights in normal condition, especially at the time of equitization.
- ii. It is difficult to collect information on completed land transaction because investors always keep secrete. In addition, provincial natural resources and environment departments cannot provide accurate value of completed land transactions. Thus, it is difficult to identify the market value of land use right.

In order to facilitate equitization in the forth-coming time, the Government needs to adjust land policies in relevance to practice in Vietnam.

### ***3.3. Policies on employees, salaries and social insurance***

#### ***Preferences for employees in equitized enterprises***

Employees of SOEs that are selected for equitization receive some special treatment from the government following equitization. Specifically, they will be entitled to buy a maximum of 100 shares (VND 10,000 for each) for each year they have worked for the SOEs at a 40 percent discount on the basis of an average auction price. Especially, since 2005 these shares are freely transferred regardless of how long they are kept. Moreover, the employees will be retrained if their skills are not suitable to work for the newly-equitized enterprises. Finally, employees who are laid-off as a result of the equitization process will receive lump-sum compensation from the government.

#### ***SOE reforms and the issue of redundant workers***

Like many other countries in the world, inefficient labor utilization is one of main features of the public sector; therefore, addressing the issue of redundant workers is one of the first tasks of SOEs in reforms and renovations to enhance their efficiency and competition in the context of trade liberalization.

Up to date, the restructuring of redundant workers in SOEs has experienced three main stages.

*Phase 1 (1990-1993):* this was the most difficult period of Vietnam in economic transition process with low economic growth, high inflation rate and the system of laws and institutions related to labor and employment were incomplete. In this period, the Labor Code was not formulated. To solve the difficult situation of SOEs, contributing

to strengthen and develop public sector, the Ministers' Council (the Government) issued Decision No. 176-HĐBT dated October 9<sup>th</sup>, 1989 concerning some special directions and measures to reorganize labor in State owned enterprises in two years of 1989 and 1990. This Decision played a very essential role in changing the philosophy in labor area and provided breakthrough measures for SOE to develop.

*Phase 2 (1994-1997):* In this period of time Vietnam continued its reform on the basis of newly issued regulations that are more suitable with socialism-oriented market economy. In June 1994, the National Assembly passed the Labor Code that came into effect on January 1<sup>st</sup>, 1995. The reform took place mainly through merger, full accountability, lease or, in the case of prolonged loss making, dissolution and liquidation. The equitization of some SOEs also began. redundant workers are dealt with according to the Labor Code and Social Insurance regulations.

*Phase 3 (1998 to present):* The SOE reform has been implemented by speeding up the equitization process. This is a very radical reform of SOEs in Vietnam. SOEs are reviewed and classified to match suitable reform measures. The main measure is equitization, strong reduction of the number of small-scale and loss making enterprises and forming large and strong enterprises (SCs). During the reform process a substantial number of workers who did not meet work requirements became redundant, estimated at 350,000 people. The government issued Decision 41/2002/NĐ-CP on April 11<sup>th</sup>, 2002 providing policies on redundant workers due to SOE reorganization. The Government further issued Decision 110/2007/NĐ-CP dated 26/6/2007 on policies for redundant workers due to the reform of SOEs (including equitization, decentralization, sell, conversion into limited liability company, dissolution and bankruptcy). This was also a case solution to assist enterprises in the field of labor in the reform, especially in equitization and full participation in the labor market on the same footing as other enterprises

### *Results*

Regarding labor redundancy, a total of 700,000 workers were laid off during 1988-1992 in accordance with Decision No. 176-HĐBT and Decision 315-HĐBT. According to the report on the implementation of Decision 176-HĐBT, a total of 550,330 workers received some form of settlements as of December 1999 as follows:<sup>26</sup>

- 60,989 workers received pension, accounting for 11.03% of total redundant workers dealt;
- 40,651 workers were entitled to benefits of working ability loss, making up of 7.39%; and

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<sup>26</sup> ILSSA, 2008: Impact of the Globalization, Industry Restructuring, Labor Market and Worker's Benefits. IDRC.

- 448,981 workers received severance pay, equivalent to 81.58%.

A majority of redundant workers moved out of the State sector, found job and had stable income. There was no major social change. However, according to a survey of MOLISA, about 30 percent of them was still in difficult situation and needed assistance from other socio-economic programs, including vocational training, credit from the State fund for employment, and the national target program for hunger eradication and poverty reduction.<sup>27</sup>

For the number of SOE workers laid off in Phase 2 and 3 in accordance with Decree 41/2002/ND-CP and Decree 110/2007/ND-CP, 239,025 workers in 3,758 SOEs were settled with total cost of VND 7,808 billion. In 2007, 39,608 SOE workers were resolved at the cost of VND 1,384 billion..

**Table 2. Social protection for redundant workers from SOEs**

<b>Year</b>	<b>Total workers received support</b>	<b>Number of SOEs received support</b>	<b>Total cost (VND million)</b>	<b>Average allowance per redundant worker (VND million)</b>
2002	1,147	34	29,262	25.5
2003	18,445	453	534,973	29.0
2004	43,659	873	1,298,738	29.7
2005	86,483	1,445	2,812,933	32.5
2006	49,683	953	1784,329	35.2
2007	19,401	367	948,616	48.9
<i>Total</i>	<i>218,818</i>	<i>4125</i>	<i>7, 372,851</i>	<i>33.7</i>

*Source:* Vietnam Development Report 2008.

### *Labor redundancy in the context of globalization and international economic integration in the next period*

In the next few years the settlement of labor redundancy will be two folds: (i) under the pressure of transition from a central planning economy to a market economy, SOEs must operate according to the principles of full accountability, reorganize its labor force and set new requirements for the labor force, etc. all of which will lead to labor redundancy; and (ii) the globalization and international economic integration force SOEs to renovate technology and restructure its work force shifting the demand to more skilled workers.

Moreover, in the context of globalization and international economic integration, factors such as economic crisis (whether global, regional or domestic), price dumping and anti-

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<sup>27</sup> Ibid.

price-dumping law suits, too hot economic growth, inflation and foreign commodities dominating the domestic market, etc. threaten the existence of enterprises. Enterprises that cannot withstand the competition will go bankrupt (small and medium enterprises, and vulnerable industries such as garment, leather, etc).

The government has been playing its "midwife" role through introducing active and passive labor market programs. As a result, (i) the labor market has been formed and is growing; the share of wage earners has been continuously increasing; the labor market infrastructure is being completed; (ii) a rather complete and comprehensive set of regulations facilitating the development of labor demand and human resource (enterprise law, land law as well as policies supporting enterprises and law on education and vocational training) has been formulated; (iii) programs supporting employment, hunger eradication and poverty reduction, such as National Employment Fund 120, National Target Program for Poverty Reduction, and other passive programs such as Unemployment Insurance Law effective since January 1<sup>st</sup>, 2009, the Voluntary Social Insurance Law, etc. have been effectively supporting workers and helping them reenter the labor market.

It is estimated that 120,000 workers in SOEs will lose jobs in the next several years. An approved plan foresees that 1,553 SOEs will be restructured during 2007-2010. By the end of 2010 there will be a total 745 SOEs and 60 corporations with the government as majority shareholder. So, redundancy will still be an important issue.

### ***3.4. Credit policies***

Vietnam had around 12,300 State-owned enterprises (SOEs) at the beginning of Doi Moi. Economic performance of SOEs lagged as they lacked incentives to be more efficient and profitable. Accumulated bad debts of unprofitable SOEs, resulting in a mounting fiscal burden and budget deficits, have always caused headaches for the government.

In November 2004, the government issued Decree No. 187/2004/ND-CP, replacing Decree No. 64/2002/ND-CP. This Decree helps overcome problems related to SOE's bad debts (both receivable and payable). According to Decree 187, equitized companies will receive preferential treatment from the Government with the entitlement to borrow from State Commercial Banks (SCBs) and other State financial organizations using the same mechanisms and interest rates that are applied to SOEs.

Up to date, State Commercial Banks has been the largest lender of SOEs. There are several reasons, including the traditional relationship between SCBs and SOEs, having the same form of ownership, large borrowing demand SOEs and high lending capacity of SCBs.



There have been no official reports as well as data on outstanding loans of SOEs in commercial bank. However, individual bank has rather complete data on loans of each SOE.

Loans to SOEs by the end of 2005 were at VND 42,170 billion<sup>28</sup> (47.6% of the total outstanding), but the figure has dropped to VND 41,500 billion in June 2006 (41%).

Commercial banks have been targeting private enterprises, especially small-and-medium-sized companies, instead of SOEs, a major departure from the past when SOEs were the main clients. In 2006, Total outstanding loans to SOEs accounted for 70-80%.

Representatives the banking sector said it is risky to lend to SOEs because most are in “bad financial situation” and have no assets mortgaged for their loans. The State Bank of Vietnam’s Credit Information Centre (CIC) also forecasted a gloomy picture for them. Among the 5,199 State-owned companies that submitted financial reports for 2004, those ranked AAA and BBB (‘good’ and ‘very good’) were only at 17.1% and 18% respectively, where the figures were 44.1% and 45.4% for foreign invested enterprises and 31.2% and 27.6% respectively for limited and joint stock companies.

Commercial banks classify SOEs into three groups by their status of overdue loans as follows:

- i. Transportation Construction Corporations under the Ministry of Transportation.  
In 2007, it was estimated that total loans of these Corporations reached more than VND 12,300 billion, mainly consisting of bad debts.
- ii. Some Construction Corporations under several ministries, sectors and localities.  
Bad debts of this business group were estimated to be more than VND 2,000 billion.
- iii. Local SOEs which are administered by province and city governments. Bad debts of this group might also reach VND 2,500-3,000 billion.

It can be seen that bad debts is one of the constraints for the process of SOE equitization.

### **3.5. Tax policies**

According to Decree No. 187/2004/ND-CP, equitized companies will receive preferential treatment from the government. The main preferences as follows:

- preferences with respect to the enterprise income tax in line with any newly-established enterprises (in the normal case, the enterprise is exempted from income

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<sup>28</sup> <http://english.vietnamnet.vn/biz/2006/06/583697/>

tax for the first two years and a 50 percent reduction of income tax for the third and fourth year after equitization);

- exemption from the registration fee for registered assets of the new companies;
- compensation for equitization expenses from the proceeds.

In November 2007, the Ministry of Finance issued Circular No. 134/TT-BTC guiding the implementation of Decree No. 24/2007/ND-CP dated February 14, 2007 of the Government. According to this Circular, existing regulation that the enterprise is exempted from income tax for the first two years and a 50 percent reduction of income tax for the third and fourth year after equitization was dismantled.

The Ministry of Finance explained that the above-mentioned had encouraged and speeded up the equitization process but in the following years, SOEs to be equitized are large in scale and operate effectively with significant market share and trademarks recognized. Therefore, if this preferential policy were continued, it would be unfair for newly established enterprises and lead to loss of State revenue.

## **PART II. RESULTS OF STATE-OWNED ENTERPRISE REFORMS AND RENOVATIONS**

### **1. The number of enterprises whose ownership and type have been transformed**

The simultaneous implementation of SOE reforms previously mentioned in Part I has produced better results over time. Until the end of 2008, the number of SOEs whose ownership and type have been transformed stood at 5,408, 71% of which have been equitized and transformed into shareholding companies; the majority of the remaining ones have been transformed into one-member limited liability companies in which the State retained 100% chartered capital. These transformed enterprises comprised those under provincial management (64.7%), those under ministries' management (over 25%), and member companies of SCs of 91-type under Central management (nearly 10.3%).

**Table 3. The number of SOEs implementing reforms and renovations until 12/2008**

Management bodies	Number of SOEs	Number of equitized SOEs
Total	5406	3836
Ministries, branches	1354	1164
Corporations 91	554	440
Locals	3498	2232

*Source: Ministry of Finance.*

### **2. Results of SOE equitization**

Equitization, as a measure of SOE reform, can take one of the following four forms: (i) keeping State shares intact and issuing new shares; (ii) selling part of the existing State shares; (iii) detaching and then selling parts of an SOE (a method mostly applied to State Corporations); and (iv) selling off all State shares to workers and private shareholders (a method mostly applied to loss-making SOEs).

The following issues are defined in the government's policy on the SOE reform as objectives of the equitization program:

- Improving the performance and competitiveness of enterprises by converting the enterprises that the State does not need keep 100 percent of capital to form of enterprises with numerous owners;
- Mobilizing capital from employees and outside investors, including domestic and foreign investors, for renewing technologies and developing enterprises' business;

- Promoting the real owner role of employees, shareholders and the social supervision over enterprises; and
- Balancing interests of the State, employees and shareholders in the equitized enterprise.

Through more than 16 years of execution, the equitization of SOEs acquired several main achievements. The actual legal framework of equitization has defined more clearly the objectives of equitization, widened the scope of equitized enterprises in terms of business activities and enterprise scale, enlarged the scope of subjects having the rights to buy shares for the first time, and allowed using different methods to evaluate the enterprise value.

The equitization is considered as the main solution in the reforms and renovations of SOE sector. It is reported that, by December 2008, there were 5,406 out of about 6,200 SOEs implementing reforms and renovations, of which, 3,836 SOEs were equitized with more than 10 State Corporations and 60 enterprises with more than VND 100 billion of chartered capital, accounting for 71 percent of total reorganized SOEs. Through equitization, VND 100,000 billion were mobilized from domestic and international individual and institutional investors by buying shares of equitized enterprises. According to National Steering Committee for Enterprise Renovation and Development, in 2007, Hanoi and Ho Chi Minh Stock Exchange organized auctions for 96 SOEs with total chartered capital of nearly VND 54,000 billion, the number of shares dealt made up 92% of total shares offered.

According to the Ministry of Finance, by the end of 2007, nearly 20 percent of the State capital was equitized.<sup>29</sup> The State holds 52 percent of total shares while 21 percent and 27 percent of total shares belong to the employees and other types of owners, respectively. The number of equitized enterprises with more than 50 percent of State share accounts for 33 percent of total equitized ones.

Until 2007, the proportion of equitized enterprises by forms of equitization was as follows:

- |   |        |
|---|--------|
| - Keeping State shares intact and issuing new shares:               | 15.1%; |
| - Selling a part of State shares and issuing new shares:            | 69.4%  |
| - Selling off all State shares to workers and private shareholders: | 15.5%  |

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<sup>29</sup> Le Song Lai, 2007: SOE reform in Vietnam - Progress report.

At the end of 2008, the amount of State capital in equitized enterprises under SCIC's management has increased by 26%; chartered capital by 36%; enterprises' revenues by 44%; and enterprises' profits by 105%<sup>30</sup>.

Besides achievements gained, there are still many outstanding problems related to equitization. Most of equitized enterprises are small in scale and the pace of equitization is still low. Among 4,000 equitized enterprise, the number of enterprises with more than VND 5 billion only accounts for nearly 40%. Although several large-scale SOEs were equitized in the last three years, only 23-30% of total State capital was equitized.

According to the plan approved by the Prime Minister, in 2007 - 2010, 1,533 SOEs nationwide will be reorganized, of which 950 SOEs will be equitized. Statistics of the Ministry of Finance show that there were 1,192 SOEs which have not been rearranged by the end of 2008 while the Government set the target of maintaining 700 to 800 SOEs after 2010. However, in 2007, there were only 271 SOEs implementing reforms and renovations out of targeted 550 ones, of which 116 SOEs were equitized. That means, in 2009 and 2010, 750 SOEs will need to undergo equitization in order to complete the plan but this seems to be a long way to go.

The equitization has been partial and internal as the State and insiders (including managers and employees) holds the largest proportion of shares and only 27% of shares have been sold to the outside investors. There is a problem of information asymmetry between insiders and outsiders with respect to real and future value of equitized firms. The upper limits on share ownership imposed on both domestic and foreign individual and institutional investors make internal equitization even clearer. This is also a reason why it fails to mobilize capital from employees and outside investors, including domestic and foreign investors, for renewing technologies and developing enterprises' business.

Equitized enterprises have been undervalued because (i) the value of land use rights has not been properly accounted for; (ii) valuation of enterprises is subjective as it is the result of negotiation between the managers and the evaluation committee or the auditing firm<sup>31</sup>; and (iii) equitization has been mostly internal because managers of profitable SOEs have incentives to keep it as such. At the same time, outside investors are unwilling to assume the risk needed to break this internal inertia of equitization.

As the equitization process in Vietnam has many shortcomings. Only systematic and comprehensive measures can properly address these problems.

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<sup>30</sup> Vietnam News Agency, posted on the OTC Stock Exchange website: <http://news.sanotc.com>.

<sup>31</sup> Decree No. 187/2004/ND-CP of the Government dated November 16<sup>th</sup>, 2004 on conversion of SOEs into shareholding companies.

### 3. Results of transferring, selling, business contracting, leasing, dissolving or transforming SOEs into one-member limited liability companies

The number of SOEs transferred, sold, contracted out, leased, dissolved or transformed into limited liability companies with one or more than one members accounted for only a small proportion in the total of 5406 reformed enterprises. This can be seen in the following table:

**Table 4. The number of SOEs implementing reforms and renovations in 2008**

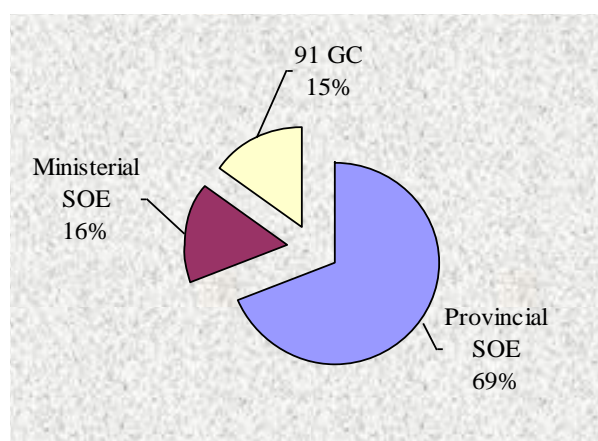
Manage – ment bodies	Equitize	Trans- fer	Sell	Dis- solve	Farms and plantations transformed into companies	One mem. Ltd., com- pany	Two mem. Ltd., com- pany	Parent com- pany	Total
Ministries, branches	24	0	0	0	0	8	0	0	32
Corporations 91	8	0	0	0	0	0	0	0	8
Local	52	1	3	3	7	23	1	1	91
<b>Total</b>	<b>84</b>	<b>1</b>	<b>3</b>	<b>3</b>	<b>7</b>	<b>31</b>	<b>1</b>	<b>1</b>	<b>131</b>

*Source: Ministry of Finance.*

Due to their unsuccessful outcomes, business contracting and leasing SOEs have been phased out since 2008, and been replaced by auctioning SOEs. Of the 131 enterprises implementing reforms in 2008, the majorities were equitized; one was transferred, and three were sold. Despite its slight improvement compared with previous years, this outcome was still considered disappointing.

The transformation of SOEs with 100% State chartered capital into one-member limited liability companies operating in compliance with the 2005 Enterprise Law has been accelerated since 2006 and targeted SCs and independent State companies. At the end of 2007 there were approximately 322 SOEs implementing this type of transformation, most of which were those under local management.

**Figure 1. Composition of SOEs that were transformed into one-member limited liability companies at the end of 2007**



*Source: CIEM (2007).*

The number of SOEs transformed into one – member limited liability companies rose to 31 at the end of 2008, 23 of which are under local management and the rest is under ministerial management. It should be noted that in the two years 2007 and 2008, there is no SCs transformed into one-member limited liability company, even though the deadline of this mandatory transformation is July 1<sup>st</sup> 2010 according to the Law on Enterprises 2005.

#### **4. Results of transforming State Corporations into the parent-subsidary company model and establishing business groups**

During the period 2004-2007, Vietnam had 120 SCs, BGs and large-scale independent State companies<sup>32</sup> that had been organized and operated under the model of parent-subsidary company<sup>33</sup>. In 2008, there was one more SC of 90-type restructured and transformed under this model. The transformation of large-scale SOEs and SCs into the parent-subsidary company model, in which the relationship amongst members is based on their association in capital, technology, and markets, has had positive impacts on the performance of transformed SOEs. The separation and distinctness of responsibilities, powers, interests between parent and subsidiary companies have made these companies more closely interacted in order to gain mutual benefits, while respecting each other's independent function.

BGs in Vietnam have the following main characteristics:

<sup>32</sup> In mid-2008, the total state capital of 7 BGs, 11 SCs of 91-type and 56 SCs of 90-type were estimated to attain VND 402.815 billion, 73.6% of which were accounted for by BGs and SCs of 91-type (CIEM, 2008).

<sup>33</sup> CIEM, 2008: Vietnam's Economy in 2008.

▪ *Ownership structure:* BGs operate in the model of parent-subsidary company. Of eight parent companies, seven were SOEs with 100% State chartered capital. In contrast, the majority of subsidiary companies and member enterprises are owned by multiple holders due to implemented reforms, including equitization. This is a notable characteristic of BGs. The following table shows that not only BGs have many members, but their members also have various enterprise types and ownership structures themselves. The most common type of BGs' member companies is shareholding company.

**Table 5. Number of member enterprises in BGs in 2008**

BGs	Number of subsidiary companies				Affiliated companies	Non-business units
	State companies	One - member limited liability companies	Share-holding companies ( parent company has >= 50% chartered capital )	Limited liability companies		
Vinatex (T&G)	2	3	15	0	49	0
TKV (Coal&Minerals)	14	7	36	4	17	5
EVN (Electricity)	8	9	24	0	20	5
Vinashin (Shipbuiding industry)	1	15	25	0	19	2
VNPT	1	1	8	0	21	7
Petro Vietnam (Oil&Gas)	0	7	14	1	1	2
VRG (Rubber)	23	0	32	0	16	4

*Source: Tran Xuan Lich<sup>34</sup> (2009), Table 1.*

▪ *Scale and areas of economic activities:* The eight BGs established in piloting are all large-scale SOEs, playing a leading role in key economic sectors as well as in supporting the Government to stabilize macro-economic environment and markets. Since its launch, Petro Vietnam has contributed to 25-30% of State budget; TKV has supplied over 97% of domestically consumed coal; EVN has produced 94% of the nation's electricity output; Vinashin has been the key player in Vietnam's shipbuilding industry; Vinatex has made up 18% of export revenues of all industries, etc.

▪ *Organization and management:* The organization structure of BGs is mainly based on the relationship between parent and subsidiary/member companies and is formed in accordance with their areas of economic activities and international practices. In addition, member companies in several BGs have been restructured towards specialized production.

<sup>34</sup> Report at the Conference on Business Groups: Theory and Practice organized by the National Political Publishing House, CIEM, Vietnam Economic Times, Vietnamese Youth Company in Hanoi, May 2009.



After transformed from SCs, all BGs have a parent company and various types of member companies, including: (1) subsidiaries, all of whose chartered capital is owned by its parent company; (2) company held controlling proportion of capital contribution or share by the parent company; and (3) affiliated companies. In a BG, the parent company plays a core role in associating member companies and holds a controlling right over them. All of the eight State BGs do not have a top management body for both parent and member companies, but rather use the parent company's management system to manage and supervise the entire BG. Rights of owners and shareholders are fulfilled pursuant to the Enterprise Law. Business contracts between parent company and affiliated companies demonstrate the constitute the basis for the parent company to control and orient the function of member companies towards common strategic goals.

Most of these eight BGs have formed affiliated relationships in accordance with their business characteristics. Parent company not only engages in business activities directly, but also plays a key role in developing business strategy; regulating business plans and resources' usage; utilizing available services amongst member companies and outside organizations to attract more investment and business contracts. In addition, parent company is able to seek capital from various sources and guarantee for its member companies to borrow loans with prior conditions. Parent company also organizes training courses and guides to human resource management; orients R&D activities and applies into production. The relationship between parent and member companies as well as amongst member companies themselves are enforced based on the signed business contracts.

Several BGs have organized their member enterprises as specified groups in which those members in certain groups are specialized in one industry, i.e. accelerate production specialization within BGs. For example, Petro Vietnam established subsidiary SCs under the model of parent-subsidiary company, each of which operates in a different area such as oil and gas exploration and exploitation; drilling and drilling services; gas, nitrogenous fertilizer production; etc. Similarly, VNPT separated its postal service to form Vietnam Postal Corporation (VPC); or EVN separated out its power transmission function to form the National Power Transmission Corporation (NPT). Thus, one BG can form multi-level subsidiary SCs operating under the parent-subsidiary company model.

## **5. Production and business efficiency of business groups and enterprises that are equitized and transformed into one-member limited liability companies**

After equitized<sup>35</sup>, the majority of enterprises have reported higher business efficiency, which is evaluated based on changes in chartered capital; the number of newly-created jobs; employees' income; productivity; and production and business profit in proportion to owner' capital.

### *Changes in chartered capital*

The total chartered capital of equitized enterprises are 1.5 times the amount of State capital in these enterprises at the time of equitization. Up to December 31<sup>st</sup> 2007, on average, the State capital comprised 52% chartered capital in equitized enterprises; 21% held by enterprise's employees and the rest of 27% by outside investors<sup>36</sup>. However, with the regulations on the minimum percentage of shares held by outside buyers when equitizing and policies for promoting strategic investment, the proportion of shares kept by outside shareholders has surged in recent years. In 2007, for example, outside shareholders owned 40.31% chartered capital in an equitized enterprise while the State held 44.17% and enterprise's employees held 15.52%.

### *Changes in the number of employees*

In general, the number of new employees in equitized enterprises increased each year. From 2005 to 2007, the increase in the total number of employees of these enterprises had leaped from 8,264 to 27,453 people. The number of laborers in equitized enterprises with controlling proportion of State capital has increased faster than that of in shareholding companies without controlling proportion of State capital. In the former, most of the new laborers are in Central shareholding companies<sup>37</sup>, especially in 2007. Yet this does not show that central shareholding companies are more efficient than other types of shareholding companies.

In contrast, the number of employees in State companies has decreased. For 3 years, there had been nearly 30 thousands redundant employees due to lay-off policy (almost 46%) and the restructure of State companies. Since 2006, State companies transformed into one-member limited liability companies have increased the number of employees in their labor force.

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<sup>35</sup> The most popular mode of equitization is to sell part of state capital in enterprises, while issuing new shares (almost 70%). The mode of selling all state capital in enterprises accounted for around 15%,; that of maintaining state capital in enterprises while issuing new shares made up the rest (around 15%) (SCERD, 2008).

<sup>36</sup> SCERD, *Report on SOE reorganization and renovation, and the program and plan for 2008-2010*, Conference on April 23<sup>rd</sup> 2008.

<sup>37</sup> Shareholding companies in which the Central Government holds a controlling proportion of share

**Table 6. Changes in the labor force of equitized State-owned Enterprises**

Types of enterprises	2005		2006		2007	
	<i>No. of enterprises</i>	<i>No. of employees</i>	<i>No. of enterprises</i>	<i>No. of employees</i>	<i>No. of enterprises</i>	<i>No. of employees</i>
State companies	2769	-27659	1973	-8961	1503	-1720
- Central	1131	-7635	841	4788	645	3694
- Provincial	1638	-20024	1132	-13749	858	-5414
State limited liability companies	250	-197	382	4945	471	7729
- Central	75	-98	114	2027	142	4167
- Provincial	175	-99	268	2918	329	3562
Shareholding companies with controlling proportion of State capital						
- Central	914	2963	1201	7183	1360	14233
- Provincial	476	3126	645	3507	779	11133
	438	-163	556	3676	581	3100
Shareholding companies with non-controlling proportion of State capital						
	1531	5301	1666	8268	1929	13220

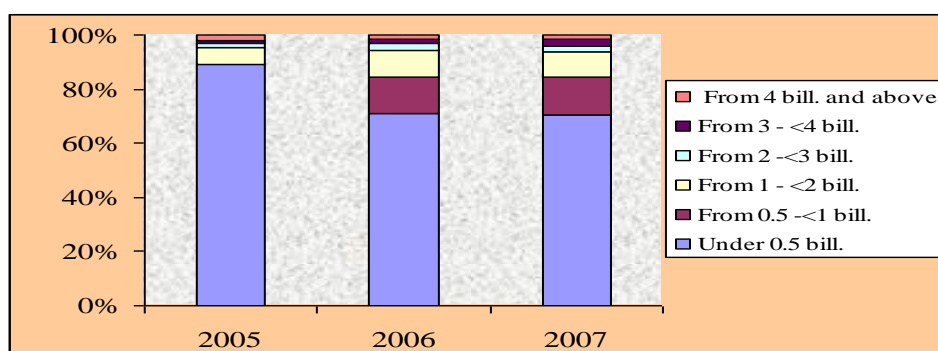
*Source: Calculations based on data from the Enterprise Surveys 2005-2007 by GSO.*

### *Changes in productivity<sup>38</sup>*

In general, the average productivity of enterprises whose ownership or administrative model had been transformed increased each year. In 2007, 70.4% of these enterprises had their productivity under VND 0.5 billion; the figure in 2008 mounted up to 80.6%. In addition, the share of enterprises with productivity between VND 0.5 billion and 2 billion in total enterprises has rocketed (see Figure 2). The number of enterprises with average productivity of more than VND 4 billion did not seem to change in three years 2005-07.

<sup>38</sup> Productivity is measured by dividing total revenue (by year) over number of employees on average (by year).

**Figure 2. Composition of enterprises whose ownership and administrative model have been transformed, by average productivity 2005-2007 (VND billion)**



*Source: Calculations based on data from the Enterprise Surveys 2005-2007 by GSO*

Overall, there is not much difference in terms of productivity among different types of enterprises, with equitized enterprises being slightly better. The share of independent State companies with productivity under VND 0.5 billion in total State companies is still the highest (over 80% at the end of 2007). During the period of 2005-07, the proportion of limited liability and shareholding companies with the labor productivity from 0.5 to less than 2 billion increased more than 4 percent while this remained in the State companies. In other words, there seemed to be no improvement in State companies' average productivity although their labor force had shrunk down during 2005-2007.

**Table 7. Comparison of the composition of enterprises whose ownership and administrative model have been transformed, by average productivity 2005-2007**

*Unit: Percentage*

		Under VND 0.5 billion	VND 0.5 billion - <1 billion	VND 1 billion - <2 billion	VND 2 billion - <3 billion	VND 3 billion - <4 billion	VND 4 billion or more	Total
State companies	2005	81.22	8.49	4.80	1.95	0.98	2.56	100.00
	2006	78.50	8.47	5.48	2.84	1.27	3.45	100.00
	2007	73.93	10.87	5.13	3.40	1.93	4.73	100.00
State limited liability companies	2005	82.40	9.20	4.00	1.60	1.20	1.60	100.00
	2006	82.46	8.12	4.45	1.83	0.79	2.36	100.00
	2007	80.04	9.13	4.88	2.76	1.06	2.12	100.00
Shareholding companies with more than 50% State capital	2005	77.80	10.70	5.90	3.20	0.90	1.50	100.00
	2006	75.60	11.20	7.00	2.60	1.30	2.30	100.00
	2007	70.50	13.60	7.60	3.60	2.00	2.70	100.00
Shareholding companies with no more than 50% State capital	2005	79.10	10.70	5.50	2.60	0.50	1.60	100.00
	2006	77.90	11.50	5.90	1.70	1.00	2.10	100.00
	2007	72.40	13.60	6.50	2.70	1.50	3.30	100.00

*Source: Enterprise Survey 2005-2007(GSO)*

### *Changes in employees' income*

The average income of employees in transferred SOEs tends to rise during the period 2005- 2007. In State companies, for example, the average employees' income in 2007 increased by 48.4% compared with that of in 2005. This rate in limited liability companies, shareholding companies with controlling proportion of State capital, shareholding companies with non-controlling proportion of State capital are 53.6%; 51.7% and 39.5%, respectively and all are much higher than the average rate of the entire enterprise sector (31.4%).

**Table 8. Average income of employees in State companies and reformed SOEs  
2005-2007 (VND million)**

	2005			2006			2007		
	No. of Ents	Total average empls*	Monthly income	No. of Ents	Total average empls*	Monthly income	No. of Ents	Total average empls*	Monthly income
State companies	2,752	1,476,089	2.28	1,971	1,141,744	2.97	1,500	645,238	3.38
- Central	1,119	1,003,930	2.61	840	810,447	3.45	643	408,626	3.89
- Local	1,633	472,159	1.56	1,131	331,297	1.80	857	236,612	2.49
Limited liability companies	244	97,776	2.04	373	156,685	2.39	456	189,054	3.13
- Central	74	42,675	2.31	112	72,442	2.83	133	94,289	3.69
- Local	170	55,101	1.82	261	84,243	2.01	323	94,765	2.57
Shareholding companies with State capital of 50% or above	898	317,404	1.81	1,176	441,099	2.20	1,313	484,813	2.75
Shareholding companies with less than 50% State capital	1,074	275,481	1.8026	1,349	363,044	1.93	1,554	425,714	2.51
<b>All SOEs</b>	<b>104,555</b>	<b>5,745,362</b>	<b>1.72</b>	<b>126,805</b>	<b>6,211,456</b>	<b>1.98</b>	<b>148,803</b>	<b>6,550,604</b>	<b>2.26</b>

*Source: Calculations based on data from the Enterprise Surveys 2005-2007 by GSO.*

*Note: \*:Average employee = (year-beginning number of employees+ year-end number of employees)/2.*

### *Changes in production and business results*

In 2005, restructured SOEs that suffered loss accounted for 27.4% of total restructured SOEs; this figure in 2006 rose to 29.8% (see Table 8). The situation changed in 2007 as SOEs that suffered loss only accounted for less than 1% of all restructured SOEs. However, almost half of restructured SOEs only broke even. Of those that gained

profit, 44% have their profit before tax over owner's capital<sup>39</sup> only under 5% - a quite low level.

**Table 9. Composition of responding enterprise, by profit before tax over owner's capital in enterprises 2005-2007**

		Loss	Break even	Under 5%	5- <10%	10- <20%	20- <50%	50% or more	Total
State companies	2005	18.71	0.86	37.06	14.08	12.89	11.95	4.45	100.00
	2006	16.14	0.79	37.85	13.72	14.93	11.15	5.42	100.00
	2007	6.31	4.91	67.08	8.60	5.65	3.93	3.52	100.00
Limited liability companies	2005	13.11	0.82	38.52	14.34	19.26	9.84	4.10	100.00
	2006	13.17	1.34	42.74	11.02	15.59	11.29	4.84	100.00
	2007	0.79	5.56	74.87	7.14	3.70	5.03	2.91	100.00
Shareholding companies with >50% State capital	2005	8.60	0.10	21.60	12.50	28.60	24.90	3.70	100.00
	2006	9.20	0.90	19.50	12.90	30.50	22.70	4.30	100.00
	2007	1.60	3.30	70.30	11.50	6.80	4.70	1.80	100.00
Shareholding companies with <50% State capital	2005	12.70	1.10	18.40	12.00	27.00	25.60	3.20	100.00
	2006	12.70	0.60	19.30	12.30	26.20	25.80	3.10	100.00
	2007	2.40	8.90	63.20	10.60	7.90	3.70	3.30	100.00
Total	2005	27.40	8.30	37.70	10.30	8.40	5.60	2.30	100.00
	2006	29.80	2.00	39.60	13.70	8.20	4.80	1.90	100.00
	2007	0.90	46.20	43.90	4.30	2.10	1.60	1.00	100.00

*Source: Calculations based on data from the Enterprise Surveys 2005-2007 by GSO*

*Note:* The number of enterprises that respond: 2005 (110350); 2006 (129182); 2007 (102533)

<sup>39</sup> Capital from owners, investors and enterprises, and must not be a debt. Owner's capital can include: (1) Investors' initial and additional capital contribution; (2) Additional capital contribution from enterprise's production and business activities; and (3) Other sources of owner's capital.

**Box 2: Business and production results of enterprises after equitization**

Reported results from 1,616 enterprises with at least one year of operation after being equitized (until the end of 2006) show that chartered capital increases by 58.6%; revenues 48.2%; profits 331.8%; contribution to State budget 44.2%; employees' income 51.8%; dividend 13% compared with that prior to equitization. Enterprises that suffered loss still accounted for 7.1% of all equitized enterprises<sup>40</sup>. As employees now becoming shareholders, having right to approve company charter, voting on important issues of their enterprise, the performance of equitized enterprises has seen improvements. On enterprise side, changes in corporate governance bring new mechanism of running business with higher self-control accompanying higher responsibilities to laws and shareholders, and more importantly, get rid of deep intervention from the representative bodies of State ownership.

Business results of State companies in 2007 seem to be lower than other types of SOEs. Of the four types of SOEs, State companies have the highest share of companies that suffered loss (6.31%), but also have the highest before-tax profit over owner's capital ratio (3.52%). Besides, it should be noted that the majority of SOEs whose ownership and administrative model have been transformed were still only be able to break even, or gain low profit. In addition, profit before tax over owner's capital ratio seems to indicate no clear difference between business result of shareholding companies with 50% State capital or more and that of shareholding companies with less than 50% State capital.

According to the Ministry of Finance's report in 2008, the total State capital in BGs and SCs increased by 13% compared with that of in 2007; revenues by nearly 31%; before-tax profit by 76%; payment to State budget 13%; and ratio of before-tax profit to State capital attained 28%. Capital size of BGs has increased significantly. For example, in 2008 State capital in Petro Vietnam, EVN, or VNPT rose by 13%, 11%, 13%, respectively compared with that in 2007. Several BGs have ventured out to invest abroad, such as Petro Vietnam invested in Africa or South America for oil exploration and exploitation; VRG invested in Cambodia and Laos for planting rubber trees.

Those above result analyses do not fully reflect the business and production efficiency of equitized, transformed into limited companies, or restructured SOEs (as with independent State companies)<sup>41</sup>. However, these results in some aspects demonstrate a part of the overall picture of SOE performance after transferred and reorganized. The results show a positive result for SOE reforms and renovations in Vietnam.

<sup>40</sup> SCERD, *Report on SOE reorganization and renovation, and the program and plan for 2008-2010*, Conference on April 23<sup>rd</sup> 2008.

<sup>41</sup> Making good assessments on business and production efficiency of these enterprises requires further analysis and shall not be included in the scope of this paper.

### **PART III. CHALLENGES FOR FUTURE REFORMS AND RENOVATIONS OF STATE-OWNED ENTERPRISES**

Reforming SOEs shall continue to be the core of Vietnam's economic transformation in the coming years. After 17 years of implementing equitization, Vietnam up to October 2009 still had 1,500 large-scale SOEs with 100% State chartered capital, in which there were 90 SCs and BGs. While the short-term goal of reforming SOEs is to complete the transformation of SOEs into shareholding or limited liability companies by July 1<sup>st</sup> 2010, the long-term goal is to improve the production and business efficiency of these enterprises. To achieve this goal, SOE reform process needs to resolve the following problems:

*First*, financial settlements for the 1,500 untransformed large-scale SOEs, including many BGs, SCs, and State commercial banks, are a difficult task due to the intricate relationship among them. This intricacy is reflected in debt situations of SOEs and a large proportion of these bad debts held by State commercial banks. This make the financial solution for SOE reform more difficult. In addition, the amount of budget that supports SOE reform in general and laborers in particular, continues to drop. Support funds from foreign organizations also follow the same route, as many countries and organizations have removed Vietnam from the list of countries that needs aids.

#### *Methods of equitization*

Determining the values of SOEs, especially that of land use right, business advantages and trademarks, remains a problem since these BGs and SCs in Vietnam are often large-scaled. In addition, current regulations on determining values of land use right, business advantages and trademarks are not clear and specific enough to be properly implemented. Unfortunately, there seems to be no quick solution for this problem in the coming years.

Moreover, it should be noted that the transformation of 100% State-owned capital BGs and SCs into enterprises subject to the Enterprise Law shall hardly be able to meet the deadline on July 1<sup>st</sup> 2010. Thus, these SOEs may need to be transformed into one-member limited liability companies before implementing equitization.

#### *Transformation of State companies into limited liability companies*

The transformation of enterprises with 100% State capital into one-member limited liability companies has been slowed down due to the stipulated minimum amount of chartered capital (VND 30 billion). This minimum amount is considered too high for many SOEs that are important to provincial economic development or those in the agriculture – forestry - fisheries sector in which the State needs to retain 100% chartered capital.



### *Transformation of State companies into the parent-subsidiary company model*

Since those companies becoming parent companies are all large-scaled, their transformation into parent companies, particularly through the equityization method, shall face difficulties in selling a very large number of shares. Besides, to establish BGs, SCs must transform all member enterprises into shareholding companies, one-member limited liability companies, or limited liability companies with more than one member. This process will take time and is costly by dealing with various issues, especially finance and labor aspects.

*Second*, the global financial crisis is likely to take its toll in the process of reforming Vietnamese SOEs, particularly of equityizing these enterprises since foreign investors may withdraw back their invested capital to fight the crisis in their own countries, and potential investors may reconsider the decision to buy shares from equityized enterprises in Vietnam. In addition, domestic economic downturn, which is in part due to the global crisis, will also have a negative impact on the initial public offering (IPO) of equityized enterprises.

*Third*, since its first day of trading, the Vietnamese stock market has seen many abnormal fluctuations, which had an adverse impact on the equityization of SOEs. The majority of investors seem to be interested only in listed shareholding companies and some potential enterprises (such as State commercial banks); strategic investors are too few in number. It should also be noted that most investors do not care about business prospects or long-term growth, but rather potential short-term profits. In addition, stock market regulations are in the process of completion; sanctions against acts of violating the regulations on transparency are not hard enough to stop violations such as collecting inside information from listed companies, securities firms, or powerful investors to gain profit. Violations have imposed risks on stock investment activities due to discrepant information and wrong market signals, which as a consequence shrinks investors' confidence in the stock market.

In light of the global financial crisis and domestic economic downturn, Vietnam must have clear and specific solutions during the coming years to resolve the existing problems in SOE reform.

## APPENDIX

**Table A.1. Changes in SOE equitization policy 1996-now**

	<b>Decree No. 28 issued in 1996</b>	<b>Decree No. 44 issued in 1998</b>	<b>Decree No. 64 issued in 2002</b>	<b>Decree No. 187 issued in 2004</b>	<b>Decree No. 109 issued in 2007</b>
<b>Goals</b>	<ul style="list-style-type: none"> <li>▫ Mobilize capital from staff and workers in enterprises; domestic and foreign individuals or economic organizations</li> <li>▫ Provide opportunities for capital contributors and employees to become shareholders, thus giving them incentive to help improve business efficiency.</li> </ul>	<ul style="list-style-type: none"> <li>▫ Mobilize capital from the whole society, including domestic and foreign individuals or socio-economic organizations</li> <li>▫ Renovate management methods; give out incentives for enterprises to improve business efficiency; increase State asset value; boost up employees' income.</li> </ul>	<ul style="list-style-type: none"> <li>▫ Enhance the efficiency and competitiveness of enterprises; form enterprises owned by multiple holders; create incentives and dynamic management mechanism for enterprises to better manage and utilize State capital and assets</li> <li>▫ Mobilize capital from domestic and foreign individuals or socio-economic organizations</li> <li>▫ Strengthen investors' monitoring over enterprises</li> </ul>	<ul style="list-style-type: none"> <li>▫ Transform SOEs in which the State did not need to keep 100% of its invested capital to enterprises owned by multiple holders; mobilize capital from domestic and foreign individuals or socio-economic organizations</li> <li>▫ Balance the interests of the State, enterprises, investors and employees</li> <li>▫ Ensure publicity and transparency of implementation with respect to market rules; avoid "closed" equitization (just within enterprise members) while developing capital and stock markets.</li> </ul>	<ul style="list-style-type: none"> <li>▫ Similar to Decree No. 187/2004/ND-CP</li> </ul>
<b>Targets of Equitization</b>	<ul style="list-style-type: none"> <li>▫ Enterprises mentioned in Article 1 of the 1995 Law on State-owned Enterprises, in which the State does not need to</li> </ul>	<ul style="list-style-type: none"> <li>▫ Similar to Decree No. 28/1996/ND-CP</li> </ul>	<ul style="list-style-type: none"> <li>▫ SOEs and their subsidiaries mentioned in Article 1 of the 1995 Law on State-owned Enterprises, which are small- and medium-sized SOEs, except those in which the</li> </ul>	<ul style="list-style-type: none"> <li>▫ State companies in which the State does not need to keep 100% chartered capital, including: <ul style="list-style-type: none"> <li>- SCs (both commercial banks and State financial organizations);</li> <li>- Independent State companies;</li> <li>- Independent cost-accounting member companies of SCs;</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▫ Independent State companies in which the State does not need to keep 100% chartered capital</li> <li>▫ Parent companies of BGs; parent companies in</li> </ul>

	Decree No. 28 issued in 1996	Decree No. 44 issued in 1998	Decree No. 64 issued in 2002	Decree No. 187 issued in 2004	Decree No. 109 issued in 2007
	retain 100% of its invested capital		State needs to retain 100% chartered capital. Results of enterprises' production and business activities are not accounted for.	- Dependent cost-accounting units of State companies	“parent-subsidiary company” groups. ▫ Independent cost- accounting member companies of SCs ▫ Dependent-cost- accounting units of State companies; BGs, SCs, parent companies and independent cost- accounting member companies of SCs ▫ Limited liability companies in which the State owned 100% chartered capital
<b>Conditions for Equitization</b>	▫ SOEs that currently have a net profit or otherwise have at least a good business prospect	▫ SOEs that have an efficient business strategy	▫ SOEs which has had a net loss for two consecutive years would be dissolved, and would not be eligible for equitization.	▫ State companies that still retain State capital (excluding value of land use rights) after deducting the following: value of assets not in use and awaiting liquidation; financial loss; devaluation of assets; unrecoverable public debts; and expected cost of equitization ▫ The equitization of dependent cost- accounting units is implemented only when the units: - meet all requirements for the enactment of an independent cost- accounting after equitization; - shall not cause any difficulty nor adverse impact for the business	▫ SOEs that still retain State capital after financial settlements and re- determination of their value

	Decree No. 28 issued in 1996	Decree No. 44 issued in 1998	Decree No. 64 issued in 2002	Decree No. 187 issued in 2004	Decree No. 109 issued in 2007
				performance of the enterprise or of other non-equitized units	
<b>Modes of Equitization</b>	<ul style="list-style-type: none"> <li>▫ The current enterprise value is maintained, while new shares are issued as stipulated.</li> <li>▫ Sell part of the existing value of the enterprise</li> <li>▫ Separate part of the enterprise that is eligible for equitization</li> </ul>	<ul style="list-style-type: none"> <li>▫ Similar to Decree No.28, with one additional form which is to sell all existing State capital value in enterprises to transform them into shareholding companies.</li> </ul>	<ul style="list-style-type: none"> <li>▫ Similar to Decree No. 44, with one additional form which is to sell part or all of existing State capital in enterprise, while issuing new shares to mobilize more funds.</li> </ul>	<ul style="list-style-type: none"> <li>▫ The current State capital in enterprises is maintained, while new shares are issued to mobilize more funds</li> <li>▫ Sell part of existing State capital in enterprises, along with, or without issuing new shares to mobilize more funds</li> <li>▫ Sell all of existing State capital in enterprises, along with, or without issuing new shares to mobilize more funds</li> </ul>	<ul style="list-style-type: none"> <li>▫ The current State capital in enterprises is maintained, while new shares are issued to increase chartered capital.</li> <li>▫ Sell part of existing State capital in enterprises, along with, or without issuing new shares to mobilize more funds</li> <li>▫ Sell all of existing State capital in enterprises, along with, or without issuing new shares to mobilize more funds</li> </ul>
<b>Buyers of Shares</b>	<ul style="list-style-type: none"> <li>▫ Economic organizations with legal status;</li> <li>▫ Social organizations recognized by law;</li> <li>▫ Vietnamese citizen 18 years</li> </ul>	<ul style="list-style-type: none"> <li>▫ Socio-economic organizations;</li> <li>▫ Vietnamese citizens, including non-resident Vietnamese;</li> <li>▫ Foreign residents in Vietnam</li> </ul>	Similar to Decree No. 44	<ul style="list-style-type: none"> <li>▫ Socio-economic organizations operating by Vietnamese law and domestic Vietnamese individuals have the rights of buy unlimited amount of shares of equitized enterprises.</li> <li>▫ FIEs, foreigners engaging in legal activities in Vietnam, non-resident Vietnamese have the rights to buy shares as stipulated by law.</li> </ul>	<ul style="list-style-type: none"> <li>▫ Domestic investors (Vietnamese individuals and socio-economic organizations established and operated by Vietnamese law)</li> </ul>

	<b>Decree No. 28 issued in 1996</b>	<b>Decree No. 44 issued in 1998</b>	<b>Decree No. 64 issued in 2002</b>	<b>Decree No. 187 issued in 2004</b>	<b>Decree No. 109 issued in 2007</b>
	old or above				have the rights to buy unlimited amount of shares ▫ Foreign investors (foreign individuals or organizations contributing capital to investment in Vietnam).

**Table A.2: Changes in the policy on transferring, selling, contracting out and leasing SOEs**

	<b>Decree No. 103 (1999)</b>	<b>Decree No. 49 (2002)</b>	<b>Decree No. 80 (2005)</b>	<b>Decree No. 109 (2008)</b>
Modes of implementation	Transfer, sell, contract out, lease SOEs	Similar to Decree No.103	Transfer, sell, contract out, lease State companies	Sell, transfer 100% State capital enterprises
Objects of transferring, selling, contracting out, leasing	A whole SOE	Similar to Decree No. 103	A whole independent State company, or a whole independent-accounting member enterprise of SCs; sell subsidiary enterprises of State companies, SCs	Transfer, sell 100% State capital enterprises, independent-accounting member enterprises of SCs
Conditions	Enterprises in which the State capital recorded in their respective accounting books is under VND 1 billion and there has been continuing loss or the State does not need to hold shares; except those that are State-run farms or plantations, or that operate in areas of consulting, designing, appraising.	Independent SOEs and independent-accounting member enterprises of SCs in which the State capital recorded in their accounting books is below VND 5 billion and the State does not need to hold shares or which cannot be equitized	<ul style="list-style-type: none"> <li>▫ Transfer independent State companies, independent-accounting member enterprises of SCs in which the State capital recorded in their respective accounting books is under VND 5 billion and the State does not need to hold shares or which cannot be equitized</li> <li>▫ Sell State companies and independent-accounting member enterprises of SCs in which the State does not need to hold shares or which cannot be equitized; subsidiary enterprises in which the State does not need to hold 100% chartered capital, and which meet all requirements for the enactment of an independent-accounting</li> <li>▫ Contract out or lease the entire State companies and independent-accounting member enterprises of SCs, whichever their respective capital size is.</li> </ul>	<ul style="list-style-type: none"> <li>▫ Transfer enterprises which : (1) have total asset value recorded in their respective accounting books under VND 15 billion; (2) do not have land advantage; (3) meet conditions for transfer as mentioned in the master plan on reorganization and renovation of State enterprises.</li> <li>▫ Sell enterprises (independent of their respective capital size) which: (1) meet conditions for sale as mentioned in the master plan on reorganization and renovation of State enterprises ratified by the Prime Minister; (2) meet conditions for equitization as mentioned in the master plan on reorganization and</li> </ul>

	<b>Decree No. 103 (1999)</b>	<b>Decree No. 49 (2002)</b>	<b>Decree No. 80 (2005)</b>	<b>Decree No. 109 (2008)</b>
				renovation of State enterprises, but cannot be equitized
Forms of transferring, selling, contracting out, leasing	<ul style="list-style-type: none"> <li>▫ Transfer enterprises to their collective employees</li> <li>▫ Sell the whole enterprise through bidding, or directly.</li> <li>▫ Lease enterprises' properties or enterprises, directly or through bidding</li> </ul>	Similar to Decree No. 103	Similar to Decree No. 103, with one additional form which is to contract out enterprises through direct negotiation or bidding	<ul style="list-style-type: none"> <li>▫ Transfer enterprises to their collective employees</li> <li>▫ Sell enterprises directly or through bidding</li> </ul>
Entities to which SOEs are transferred, sold, contracted out, or leased	<ul style="list-style-type: none"> <li>▫ Collective employees in enterprises (represented by the Executive Board of labor union) or individuals authorized by the collective employees to represent them.</li> <li>▫ Economic organizations and individuals that are not prohibited by the Enterprise Law to contribute capital (excluding FIEs)</li> </ul>	Similar to Decree No. 103	<ul style="list-style-type: none"> <li>▫ Enterprises are transferred to their collective employees</li> <li>▫ Buyers of part of entire companies are economic organizations and individuals that are not prohibit by the Enterprise Law to contribute invested capital (including FIEs)</li> <li>▫ Entities to which enterprises are contracted out or leased include individual or collective employees in enterprises; other enterprises (excluding FIEs); and individuals having business registration</li> </ul>	<ul style="list-style-type: none"> <li>▫ Enterprises are transferred to their collective employees</li> <li>▫ Buyers of enterprises include economic organizations and individuals that are not prohibited by the Enterprise Law to contribute invested capital (including FIEs)</li> </ul>

**Table A.3: Changes in the policy on the transformation of SCs after the parent-subsidary company model**

	Decree No. 153 issued in 2004	Decree No. 111 issued in 2007
Requirements	<p><u>For State Corporation:</u></p> <p>(1) All member enterprises had been or are being transformed; or the appropriate authorities have ratified its plan and list of equitization or of transformation into one-member limited liability companies having parent, subsidiary, affiliated companies.</p> <p>(2) The Prime Minister has approved that the SC is included in the list of enterprises which shall have 100% chartered capital owned by the State after transformation and operate by the Law on State-owned Enterprises.</p> <p>(3) The SC, which shall be parent company after transformation, must have large capital size, and can utilize its “real” capital sources or has a viable plan to mobilize more capital, to have enough invested capital in subsidiary, affiliated companies to be able to control them.</p> <p>(4) The SC has viable growth potential, and can conduct business activities in various areas, one of which should be the main one, having many domestic and foreign dependent units.</p> <p><u>For independent State company, independent cost-accounting member company of SCs:</u></p> <p>(5) They can be reorganized into parent companies with large capital size or parent companies that can utilize their financial capability, technological know-how, trademarks, markets to control other enterprises.</p> <p>(6) Similar to item (2) above.</p> <p>(7) They are holding a controlling proportion of capital contribution and share in other enterprises; or the appropriate authorities have ratified their plan of equitizing member units (except the unit that will become parent company), or plan of investing more than 50% of chartered capital into other enterprises in order to hold a controlling proportion of capital contribution or share in these enterprises.</p> <p><i>SCs, independent State companies, independent cost-accounting member enterprises that do not meet all of the above requirements can still be transformed into one of the following types of parent company (operating in accordance with the Enterprise Law):</i></p> <p>(8) One-member limited liability company with 100% State capital.</p> <p>(9) Limited liability company with more than one member and with 100% State capital.</p> <p>(10) Limited liability company with more than one member and with State capital contribution.</p>	<p><u>For State Corporation:</u></p> <p>(1) Similar to item (1), Decree No. 153</p> <p>(2) The SC, which shall be parent company after transformation, must meet all conditions to be transformed after the model of one-member limited liability company.</p> <p>(3) Similar to item (3), Decree No. 153.</p> <p>(4) Similar to item (4), Decree No. 153.</p> <p><u>For independent State company, independent cost-accounting member company of SCs:</u></p> <p>(5) Similar to item (5), Decree No. 153.</p> <p>(6) Similar to the (2) above.</p> <p>(7) Similar to item (7), Decree No. 153.</p>



	<p>(11) Shareholding company with 100% State capital</p> <p>(12) Shareholding company in which the State holds a controlling proportion of capital contribution or share.</p>	
Relationship between SC and member companies after transformation	<p>(1) Independent cost-accounting member companies with legal status have rights to determine their business activities but are controlled by parent company through shares, capital contribution, markets, technology, etc.</p> <p>(2) The SC, being the parent company, exercises its function as an authorized representative of State capital contribution or share in member enterprises as stipulated in the company charter and related contracts. SC shall not transfer their capital invested in independent cost-accounting member companies as well as capital and assets of these companies by the non-payment mode, except for the cases where they decide to reorganize independent cost-accounting member companies or realize the objective of providing public-utility products and services.</p>	<p>(1) Similar to item (1), Decree No. 153.</p> <p>(2) Similar to item (2), Decree No. 153. In addition, the relationship between SC and member companies is based on the percentage of SC's shares and capital contribution in member companies; the company charter; and related contracts signed between them.</p>
Types of member companies, subsidiary companies, affiliated companies	<p><u>Member units of SC:</u></p> <p>(1) SC invests all chartered capital in the following member companies: independent cost-accounting member companies; dependent cost-accounting units; non-business units; one-member limited liability companies in which SC is the owner; enterprises in which SC invests all of their capital abroad; financial companies (if applicable).</p> <p>(2) SC holds a controlling proportion of shares and capital contribution in the following member companies: shareholding companies, limited liability companies with more than one member, joint ventures, enterprises established abroad in which SC holds a controlling proportion of share and capital contribution.</p> <p><u>Subsidiary companies:</u></p> <p>(3) Companies in which the parent company (SC) holds a controlling proportion of capital contribution include: limited liability companies with more than one member, shareholding companies, companies doing joint venture with foreign companies, foreign companies.</p> <p>(4) One-member State limited liability companies in which the parent company keeps all chartered capital.</p> <p>(5) Affiliated companies in which the parent company has a non-controlling proportion of capital contribution</p>	<p><u>Member units of SC:</u></p> <p>(1) Similar to item (1), Decree No. 153.</p> <p>(2) Similar to item (2), Decree No. 153.</p> <p><u>Subsidiary companies:</u></p> <p>(3) Similar to item (3), Decree No. 153.</p> <p>(4) One-member limited liability companies in which the parent company is the owner. If there is this type of subsidiary company in the model of parent-subsidiary company, there must also be subsidiary companies in which the parent company holds a controlling proportion of capital contribution.</p> <p>(5) Affiliated companies, including: companies in which the parent company has a non-controlling proportion of capital contribution in the form of limited liability company with more than one member, shareholding companies, foreign companies.</p>

**Table A.4. Composition of enterprises annually surveyed by GSO**

Type	2005		2006		2007	
	<i>No. of enterprises</i>	<i>Percentage</i>	<i>No. of enterprises</i>	<i>Percentage</i>	<i>No. of enterprises</i>	<i>Percentage</i>
01	1,131	1.0	841	0.6	645	0.4
02	1,638	1.5	1,132	0.9	858	0.6
03	75	0.1	114	0.1	142	0.1
04	175	0.2	268	0.2	329	0.2
05	914	0.8	1,198	0.9	1,358	0.9
06	6,334	5.6	6,219	4.7	6,688	4.3
07	34,646	30.7	37,323	28.5	40,468	26.0
08	37	0.0	31	0.0	53	0.0
09	52,505	46.5	63,658	48.5	77,648	49.9
10	10,549	9.4	14,801	11.3	20,862	13.4
11	1,094	1.0	1,358	1.0	1,595	1.0
12	2,852	2.5	3,342	2.5	4,018	2.6
13	491	0.4	464	0.4	452	0.3
14	354	0.3	414	0.3	491	0.3
<b>Total</b>	<b>112,795</b>	<b>100.0</b>	<b>131,163</b>	<b>100.0</b>	<b>155,607</b>	<b>100.0</b>

*Source: Enterprise Survey 2005-2007 (GSO)*

Note:

01 – Central SOE

02 – Provincial SOE

03 – Central State limited liability company

04 – Provincial State limited liability company

05 – Shareholding company and limited liability company in which State capital accounts for more than 50%

06 – Co-operative

07 – Private enterprise

08 – Partnership company

09 – Private limited liability company, limited liability company in which State capital accounts for no more than 50%

10 – Shareholding company with no State capital

11 – Shareholding company with no more than 50% State capital

12 – 100% foreign-owned capital enterprise

13 - SOE in joint venture with foreign companies

14. – SOE in joint venture with domestic company

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### Legal documents:

- [Directive No. 84/TTG dated March 4<sup>th</sup> 1993](#) [\[details\]](#)
- [Circular No. 36/TC-CN dated May 7<sup>th</sup> 1993](#) [\[details\]](#)
- [Directive No. 658/TTg dated August 20<sup>th</sup> 1997](#) [\[details\]](#)
- [Decision No. 697/TC-QD-TCND dated October 1<sup>st</sup> 1997](#) [\[details\]](#)
- [Decision No. 140/1998/QD-TTg dated August 1<sup>st</sup> 1998](#) [\[details\]](#)
- [Decision No. 1161/1998/QD-BTC dated October 20<sup>th</sup> 1998](#) [\[details\]](#)

Decree No. 63/2001/ND-CP issued on September 14<sup>th</sup> 2001 by the Government on transforming SOEs, enterprises of political or socio-political organizations into one-member limited liability companies.

Decree No. 95/2006/ND-CP on the transformation of State companies into one-member limited liability companies.

Decision No. 58/2002/QĐ-TTg issued on April 26<sup>th</sup> 2002 by the Prime Minister promulgating the classification criteria for SOEs and State corporations.

Decision No. 155/2004/QĐ-TTg issued on August 24<sup>th</sup> 2004 by the Prime Minister promulgating the classification criteria and list of to-be-classified State companies and independent cost-accounting member companies State corporations

Decree No. 38/2007/QĐ-TTg issued on March 20<sup>th</sup> 2007 by the Prime Minister promulgating the classification criteria and list of to-be-classified enterprises with 100% State capital

Decree No. 28/CP issued May 7<sup>th</sup> 1996 by the Government on transforming several State enterprises into shareholding companies

Decree No. 44/1998/ND-CP issued on June 29<sup>th</sup> 1998 on transforming SOEs into shareholding companies

Decree No. 64/2002/ND-CP issued on June 19<sup>th</sup> 2002 by the Government on transforming SOEs into shareholding companies

Decree No. 187/2004/ND-CP issued on November 16<sup>th</sup> 2004 by the Government on transforming State companies into shareholding companies

Decree No. 109/2007/ND-CP issued on June 26<sup>th</sup> 2007 by the Government on transforming enterprises with 100% State capital into shareholding companies

Decree No. 103/1999/ND-CP issued on September 10<sup>th</sup> 1999 by the Government on transferring, selling, contracting out, leasing State enterprises.

Decree No. 49/2002/ND-CP issued on April 24<sup>th</sup> 2002 by the Government, amending and supplementing several items of Decree No. 103/1999/ND-CP issued on September 10<sup>th</sup> 1999 by the Government on transferring, selling, contracting out, leasing State companies.

Decree No. 80/2005/ND-CP issued on June 22<sup>nd</sup> 2005 by the Government on transferring, selling, contracting out, leasing State companies

Decree No. 109/2008/ND-CP issued on October 10<sup>th</sup> 2008 by the Government on the sale and transfer of enterprises with 100% State capital

Decree No. 153/2004/ND-CP issued on August 9<sup>th</sup> 2004 by the Government on the organization and management of State corporations, and on the transformation of State corporations, independent State companies after the parent-subsidiary company model

Decree No. 111/2007/ND-CP issued on June 26<sup>th</sup> 2007 by the Government on organization and management of State companies, and on the transformation of State corporations, independent State companies, parent companies into enterprises after the parent-subsidiary company model and operating by the Enterprise Law

And many others.