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► Formalization and simplified micro and small enterprise regimes: Towards reform of the Viet Nam household business legislation



► **Formalization and simplified micro and small enterprise regimes**

Towards reform of the Viet Nam household business legislation

International Labour Organization

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Formalization and simplified micro and small enterprise regimes: Towards reform of the Viet Nam household business legislation

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► Foreword

As in many developing economies around the world, informal employment is pervasive in Viet Nam and accounts for around two-thirds of the country's total workforce. Informality is recognized in the country's current Socioeconomic Development Strategy as a critical development constraint. Tackling this massive challenge and facilitating the transition from the informal economy to the formal economy requires an integrated policy approach that prioritizes in particular support for micro and small enterprises (MSEs).

In Viet Nam, the registration and formalization of millions of MSEs has been facilitated through the household business (HHB) regime, a unique legal structure centred around the family unit but exhibiting features common to sole proprietorships and general partnerships around the world. HHBs employ more than 15 per cent of Viet Nam's workforce and account for a sizeable portion of MSEs. They contribute significantly to economic growth and job creation in Viet Nam and remain a popular channel for business start-ups. However, only about a third of existing HHBs (around 1.7 million at the end of 2021) operate within the formal economy, having registered with both business and tax authorities.

Formalization of the HHB sector, through official business registration and integration into the tax regime, is hindered by various factors, including gaps and inconsistencies in the existing legal and regulatory framework. Given the high representation and importance of HHBs in Viet Nam, the Ministry of Planning and Investment (MPI) has been tasked under Resolution No.01/NQ-CP of the Government to address such legislative gaps for household businesses.

In support of MPI in this critical initiative to reform the legal framework for HHBs in Viet Nam, the International Labour Organization (ILO) conducted a global analysis of MSE regimes in order to compile and highlight sound international practices. Based on that analysis, this paper proposes concrete recommendations to better integrate MSEs in Viet Nam in the formal economy, in addition to highlighting the importance of registration systems within a comprehensive and integrated policy framework for business formalization. As well, this report presents more than 20 country examples of business registration regimes around the world which can serve as a reference for good initiatives to promote enterprise formalization.



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► Abbreviations

CIT	Corporate Income Tax
EESE	Enabling Environment for Sustainable Enterprises
EU	European Union
FYB	Formalize Your Business
GDP	Gross Domestic Product
GSO	General Statistics Office
HHB	Household Business in Viet Nam
HUF	Hindu Undivided Family
MEI	Micro Empreendedor Individual (or Individual Micro Entrepreneur)
MSE	Micro and Small Enterprise
MSME	Micro, Small, and Medium Enterprise
OHADA	Organization of the Harmonization of African Business Law
PTR	Preferential Tax Regime
VAT	Value-Added Tax
VSIC	Viet Nam Standard Industrial Classification

► Summary and key recommendations

Informal employment is widespread in Viet Nam.

According to data from the General Statistics Office (GSO), informal employment account for about two-thirds of the country's total workforce. While this magnitude of informality is not uncommon around the developing world – indeed, four in five economic units worldwide are assumed to operate in the informal economy – informality in Viet Nam is acknowledged under the country's current Socioeconomic Development Strategy as a key development constraint. Tackling this challenge is perhaps hindered by the legal structure followed by many local businesses, in particular micro and small enterprises (MSEs). This legal structure, the Household Business (HHB) regime – structured around the family unit but exhibiting similarities with sole proprietorships and general partnerships available worldwide – having allowed millions of MSEs to have accessed the formal economy, both those that have fully registered and applied for a tax code and those that have not fully completed registration procedures, has nonetheless been hurt by other legal developments over the years and is now up for revision by the Government. The legal and regulatory environment is a critical element in the overall enabling environment for sustainable enterprises (ESEE), as the ILO has long championed for under the ESEE policy framework. Accordingly, it should not be neglected. This paper thus proposes recommendations to better integrate Vietnamese MSEs in the formal economy, in addition to highlighting the role of registration regimes within a comprehensive policy framework for business formalization.

The ILO's landmark Transition from the Informal to the Formal Economy Recommendation, 2015 (No. 204) stresses the importance of inclusive entrepreneurship as part of an integrated policy approach.

It aims at the development of not only micro, small, and medium-sized enterprises (MSMEs) but also of other types of businesses such as social economic units of which HHBs, combining business and familiar elements, constitute a good example. Emanating from the ILO, the Recommendation No. 204 is naturally keen on supporting better working conditions, upholding worker rights, and generally on the creation of decent jobs, which are all potentially undermined when businesses operate within the informal economy. Business registration is therefore a stepping stone, a gateway from the informal to the formal economy, into the mainstream business environment, but one that can be managed through intermediate steps. This initially involves simplifying registration procedures, bringing together, under a coordinated, whole-of-government approach, and increasingly in digital form, different governmental agencies – including tax, social security, labour, customs, and migration authorities, amongst others – to streamline the process and incentivize all types of economic units into formally registering as (formal economy) businesses.

Business formalization strategies can be structured around core themes, but they are highly dependent on contextual factors.

This contextual element is acknowledged by the ILO's Formalize Your Business (FYB) training module, which has two components: one generic, and one country focused. While the former aims at disseminating best practices in critical areas associated with formalization policy (such as business registration, bookkeeping systems, labour laws, taxation, and social security requirements), the latter is focused on implementing procedures and the adaptation of local rules and traditions to achieve the outcomes envisioned by adopting international best practices. In this view, the specificities of HHBs in Viet Nam must not be disregarded, but they can be moulded to redress current deficiencies. In other words, while there is no one-size-fits all approach to formalization policy, there are indeed common principles that can, and should, be embraced by different countries. To begin with, regulatory improvement is one of those principles. This can assume the form of revised procedures, as introduced above, and/or information campaigns, that can be communicated and conveyed to the public through different channels, from social media to social dialogue and others. Creating incentives and ensuring compliance are key as well – the carrots and the sticks of formalization.

Policymakers should be guided by high-level goals associated with formalization policy, but the calculus supporting formalization efforts should be based on utility.

Without disregard for the grand vision of businesses adhering to the high(er) standards of the formal economy, businesses are usually more sensitive to the bargain associated with the net benefits of participating in the formal economy as well as the opportunity costs of not being part of it. From a policymaking perspective, the challenge is in establishing a balance between benefits and costs, on one hand, to incentivize businesses to leap forward, and on the other, not indulging in moral hazard. Willing businesses must accept the responsibilities arising from business registration as the trade-off resulting from the advantages of formality. As well, the government must find ways to enforce those with optimal efficiency (and minimal intrusiveness). Call it the grand bargain of formalization, whereby gains are maximized by all stakeholders, including business owners, workers, suppliers, customers, administration officials, and taxpayers. Business registration contributes not only to more inclusive entrepreneurship, but also to a more trustful business environment.

The Household Business (HHB) structure in Viet Nam is intertwined with the country's social fabric and has existed since the start of market-oriented reforms of 1986.

The regime is a familiar one and has been used by millions of Vietnamese micro and small entrepreneurs. HHBs employ more than 15 per cent of Viet Nam's workforce and account for a sizeable portion of MSEs that generate about 30 per cent of the country's GDP. However, only about a third of existing HHBs (around 1.7 million at the end of 2021) fully operate within the formal economy, with the rest lurking in the informal economy or not fully registered (in other words, officially registered but still lacking a proper tax code). This large degree of economic informality associated with HHBs stems not only from the persistence of unregistered economic activity in Viet Nam, but also from legal uncertainties arising out of different laws that, in one way or another, should be applicable to HHBs. Yet in general, the number of HHBs has continued to increase over the past years, suggesting that the alternative business regimes available to MSEs in Viet Nam are not attractive either. And despite the legal challenges of HHBs, including not being acknowledged by many laws and having been subject to multiple revisions of the governmental decrees under which they have been governed, HHBs remain popular among entrepreneurs. HHBs are currently governed by Decree No. 01/2021/ND-CP (hereinafter Decree 01).

The Government of Viet Nam is developing a new decree for HHBs to address and redress the legal deficiencies that have plagued the statute in recent years.

Among those deficiencies, there are two primary areas of concern that should be covered in the forthcoming decree: a proper definition of "household business" and delimiting the parameter of businesses and activities falling under the concept of HHBs. Currently, the legal definition applicable to HHBs stipulates that these [are] "(...) established by an individual or family household members that shall take responsibility for business operations of the household business with all of their property. If a household business is established by members of a family household, one of them shall be authorized to act as the representative of the household business. The individual applying for registration of household business, or the person authorized by the family household members to act as the representative of the household business shall be the owner of the household business" (article 79.1 of Decree 01). The boundaries of ownership and financial liability are therefore not clear.

HHBs are uncharacteristic of micro business regimes found elsewhere in the world, whereby sole proprietorships, or sole traderships, as well as general partnerships, with or without hired labour, are the most common regimes.

In these regimes, eligibility thresholds are essentially defined by business revenues (turnover) and/or the number of employees, whereas HHBs are associated with the household concept. This is an ambiguous concept, not least because, following a 2015 revision to the Civil Code, HHBs are now considered neither legal nor natural persons. This is a peculiar legal setting, one which creates very practical difficulties for HHBs such as the inability to borrow from banks and obstacles into entering civil contracts. Within the Vietnamese legal framework, there are two laws that could provide proxy definitions for the household concept: the Law on Marriage and Family, and the Law on

Land. By combining these two, a household can be defined as a group of individuals with a family relationship, based on marital, blood, or raising relationships. But this definition also raises concerns.

HHB regime should move away from the intricacies of family relationships and rest alternatively on different qualifying criteria, closer to what is found in sole proprietorships and/or general partnerships around the world.

HHBs can be established by either individuals or, collectively, by household members too. Data indicate, however, that most HHBs are owned by individuals, and that when they are created by household members [the] “person authorized by the family household members to act as the representative of the household business shall be the owner of the household business” (article 79.1 of Decree 01). However, does this mean that the authorized person is also solely responsible for all types of liabilities? Or does it mean that other household members, having surrendered HHB ownership, have not been discharged of their joint unlimited liability? Because these issues remain unclear, removing the possibility of collective registration of HHBs by household members would make (individual) ownership and liability unambiguous. The individual, being the sole registration agent and owner, would also be legally responsible for all liabilities.

Ensuring that only individuals can apply to register HHBs would simplify defining the boundaries of employer-and-employee relationships and enhance compliance with relevant labour legislation.

Any participating household member, other than the leading individual, should be categorized as employees or as co-employers (partnership). These category definitions would nudge the HHB concept further towards conventional regimes such as sole proprietorships, in the first case, and general partnerships or other types of partnerships, in the second. Any other workers in the HHB, not belonging to the household itself, would be classified as employees. With regard to employment and related legal obligations, both employers and employees in the HHB are subjected to the rights and obligations as specified in relevant legislation – including for example the Labor Code, the Law on Social Insurance, and the Law on Occupational Safety and Health. These provisions should remain untouched. However, a pending issue would remain: should there be a limit to the number of household members, now either employees or partners, allowed in HHBs? The eligibility criteria for household members within HHBs is the family unit. However, the family unit, without further qualification, can be a fluid concept, prone to rule gaming. Furthermore, in simplified business regimes found elsewhere in the world there are usually restrictions to the number of employees.

As a general principle, no economic activity should be exempt from HHB registration, while HHBs should be supported in parallel by incentives, such as a simplified tax regime.

HHBs have a long history in Viet Nam, having first emerged among artisans, craftsmen, and people engaged in agricultural activities, and more recently including non-agricultural sectors such as professional services. Perhaps because of persistent legal changes, the regime’s perimeter now determines that [households] “engaged in agriculture, forestry, aquaculture, salt production, street vendors, nomadic or seasonal businesspeople, and service providers earning low revenues are not required to apply for establishment of household businesses” (Article 79.2 of Decree 01). Not only is this inconsistent with HHBs’ past, but it also creates registration exemptions which are incoherent with formalization policies. Nonetheless, it is perfectly reasonable, following business registration, to create incentives for MSEs such as simplified tax regimes and access to welfare programs. These can replace not only income tax, but also value-added tax, integrating social insurance payments as well, via fixed fee payments or related schemes, in addition to providing for exemptions or other preferential taxation regimes for small businesses.

The threshold for exemption from income and value-added taxes in Viet Nam can be increased, with the aim of supporting low-income HHBs.

Tax benefits, either through outright exemptions or reduced tax payments, are typical and effective incentives in the realm of formalization strategies. In Viet Nam, according to Circular No. 40/2021/TT-BTC, HHBs are exempt from

income and value-added taxes below the threshold of VND 100 million (around US\$4,000). However, there is seemingly room to increase that threshold, in comparison to countries in other regions of the world. For example, in Latin America the threshold is on average four times higher as a multiple of GDP per capita than the level observed in Viet Nam. Presumptive taxation, both in the form of a turnover tax and a fixed fee payment, is also available for HHBs. Yet greater clarification is required in calculating the tax liability and tax submission, notably, within the fixed fee payment (Hoang 2023). Greater articulation between preferential taxation options and the standard corporate income tax regime should also be pursued, given that the business incentives associated with graduating from preferential taxation to standard rates in Viet Nam are unclear.

To minimize the administrative burden, HHBs should only register their primary sector of economic activity.

Under Article 89 of the existing governmental decree on HHBs, there is a requirement to register for all business lines they intend to develop. This requirement allows competent authorities to easily understand and keep track of the scope of economic activities carried out by HHBs, also facilitating a more targeted policy approach to HHBs. However, the requirement adds to the administrative burden placed upon HHBs, whenever their business lines need to be updated. Therefore, with the aim of simplifying administrative procedures, it is recommended that HHBs should only register their primary business sector based on VSIC (Vietnam Standard Industrial Classification) codes at the 4-digit level. The Decree should, nonetheless, consider the imposition of limitations of operating in non-registered business lines. At the same time, additional thought should be given to territorial restrictions. HHBs may be confined to specific geographical areas; however, from a policy design perspective, there is no specific merit in restricting an MSE to one location only.

Authorities should promote inter-agency coordination and improve the digital infrastructure to support formalization in Viet Nam.

Efforts to integrate business and tax registration are underway, yet these require strengthened inter-agency coordination. Moreover, the issuance of a new, integrated HHB identification code for newly registered HHBs is also critical. The use of digital technology is a dominant theme in today's formalization policy plate, and ignoring digital developments would risk massive misjudgement by policymakers. Evidence suggests that the adoption of e-formality is less related to the level of development of individual countries, than it is to the political will of national policymakers. And interestingly, e-formality adopters now include low-and middle-income countries, not only e-government champions in high-income economies. Today, no serious attempt at addressing economic informality can be made without the use of e-business, e-employment, and e-tax registers and various types of portals and digital channels. Therefore, in Viet Nam, policymakers should place increased focus on simplifying online registration, promoting e-governance, and producing a harmonized national database for HHBs as a launching pad for a more comprehensive MSME public policy.

Formalization policy should incentivize businesses to gradually evolve from the initial stages of mere MSE registration to the more mature stages of corporate development.

This effort requires a continuum of entrepreneurship policies, from (business) stand-up, to start-up, and eventually to scale-up as well. Having businesses registered in the formal economy is a critical step in tackling economic informality. Simplified and intermediate legal (and tax) statuses, such as those presented in this paper, are one way to achieve that overarching goal. Yet increasingly, there are other novel approaches, also aimed at tackling informality, that include actions such as targeting informal clusters while also supporting informal businesses, that might also be of interest to policymakers in Viet Nam in the future. Although these approaches are not the focus of this paper, many of the recommendations proposed (including data collection initiatives and developing e-government), would likely underpin more comprehensive and sophisticated approaches to MSME public policy. These would include the Government collaborating with MSMEs on critical productivity-enhancing support, which would naturally induce formalization rather than simply enforcing it, as well as interrelated policies like export promotion and the attraction of foreign direct investment.

► Overview of household businesses in Viet Nam

In Viet Nam, household businesses (HHBs) have existed since the Doi Moi, market-oriented, reforms of 1986. Since then, the number of HHBs has risen substantially. Initially typical among artisans, craftsmen, as well as people engaged in agricultural activities, HHBs have since been adopted in many other activities, including non-agricultural sectors, such as professional services. According to Binh (2023), it is estimated that HHBs account for more than 8.5 million workers, thus representing more than 15 per cent of Viet Nam's employed population in 2023. In general, HHBs also contribute significantly to the country's vast segment of micro and small enterprises (MSEs), which are estimated to generate about 30 per cent of GDP.

HHBs are subject to formal business registration at the sub-national level of government, yet most remain informal. Based on Binh (2023), at the end of 2021, there were 5 million HHBs in existence in Viet Nam, although only about a third of them (1.7 million) had obtained tax codes. HHBs are therefore a major conduit for economic informality, in a country where informal employment according to GSO (2023a) reached 33.6 million workers (68.5 per cent of total employment) in 2021. This evidence raises two important issues. First, being popular among individual entrepreneurs and micro businesses – the average size of HHBs is just below two people – the prominence of HHBs suggests that formal statuses have not been effective in attracting broad cohorts of workers. And second, that by promoting the transition of HHBs to formality, quick gains in formalizing the economy, could be achieved.

HHBs are not only largely informal, but they are also affected by legal conundrums. From the onset, HHBs have operated either informally or through governmental decree (i.e., Decrees No. 66/2000/ND-CP and No. 109/2004/ND-CP). According to these frameworks, up until 2020, HHBs were limited to ten employees, above which they had to register as private enterprises under the Enterprise Law. However, survey data highlighted by Binh (2023) suggest that the share of HHBs employing more than 10 workers, at above 10 per cent of the total, is not negligible, and therefore that restriction has been dropped since 2020. Yet, the legal conundrum does not stop there. Indeed, despite being formally recognized by social security authorities – HHBs are considered employers under the 2014 Social Insurance Law, and subject to mandatory social contributions on behalf of employees – HHBs are now no longer recognized by the Civil Code (following its 2015 revision). Thus, HHBs are now considered neither legal nor natural persons. This is a peculiar legal setting, one which creates very practical difficulties for HHBs such as the inability to borrow from banks and obstacles into entering civil contracts.

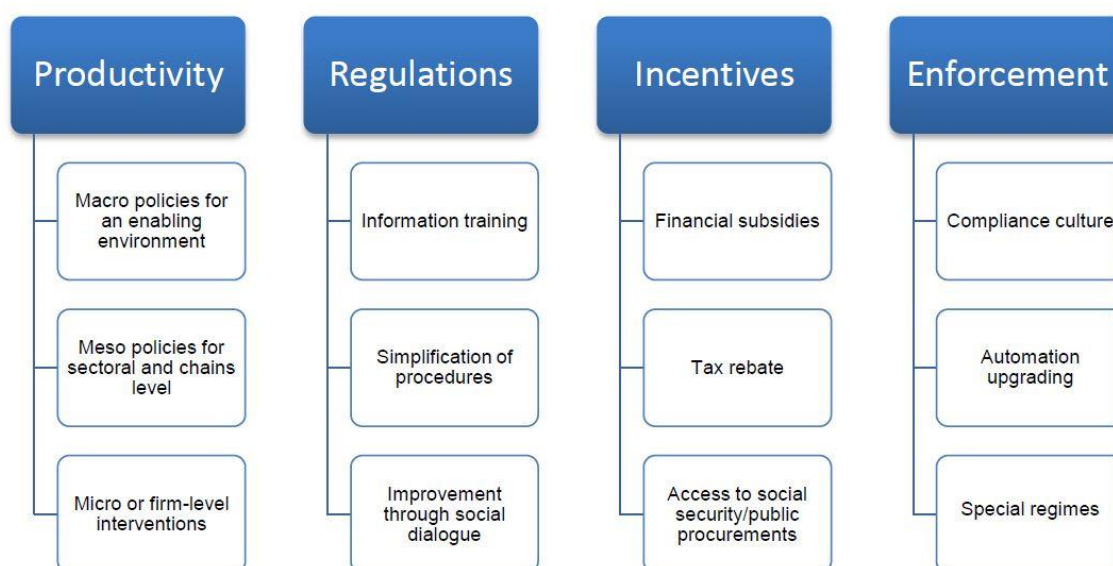
HHBs would likely welcome legal and regulatory clarification. Existing laws and regulations are internally incoherent. However, it would be highly unproductive to rule out and disqualify such a large segment of Viet Nam's business demographics, also considering that HHBs are enshrined in the country's social fabric. Already, many of them have formalized, actively contributing to social security and fiscal coffers, although below their full economic weight. The draft Decree on HHBs, currently under discussion, provides an opportunity to reassess the regulatory landscape on which these businesses operate. To this end, this section of the report looks at international experiences on business registration, not only in terms of the procedures applicable to comparable business statuses, but also through a wider policymaking perspective.

This section aims at informing policymakers on key aspects on HHBs business registration and closely related policies that should be considered when formalizing micro businesses. Specifically, should micro business regimes be devoted to own-account workers and individual entrepreneurs or, otherwise, to those employing a few workers as well? Should accounting for employees be managed upon registration? How should eligibility thresholds be designed, and how should graduating into normal, general business regimes be processed? Should there be boundaries, in terms of territorial criteria or within sets of eligible activities, restraining micro businesses under preferential, targeted regimes? These are issues that are not exclusive of HHBs in Viet Nam, and therefore international experiences can, and should, be of reference to Viet Nam's policymakers.

► What drives formalization?

Legislative efforts to facilitate and ease the registration of HHBs would help address the widespread informal economy, a stated development challenge identified in the ten-year Viet Nam Socio-Economic Development Strategy. The transition from the informal to the formal economy should be supported by governments through integrated policy frameworks. This is the main message arising out of the ILO Transition from the Informal to the Formal Economy Recommendation, 2015 (No. 204). Policy frameworks to improve the breadth and depth of the formal economy, or, in other words, to improve its attractiveness and inclusiveness, should thus target multi-dimensional aspects of overall public policy. These include the legislative and regulatory edifice overseeing the business environment; employment markets and labour relations; access to finance; access to education, infrastructure, and technology; among many others. The end goal being to provide participants in the formal economy with opportunities to benefit from, at reasonable cost, the process of formalization.

► **Figure 1: Main strategies used for the transition to formality**



Source: As in Bhattarai (2018).

The road towards formalization is a long one. Despite many countries promoting formalization policies, most businesses, globally, remain informal. According to ILO studies (Van Doorn, 2018; ILO, 2021a), roughly four fifths of the world's so-called economic units are informal. This situation is most prevalent among the very smallest of those economic units, in other words, own-account workers and microbusinesses, in addition to small-sized enterprises. The question is then: why are informal businesses insensitive to government policies, nudging and frequently guiding them into the formal sector? The answer to this question is not a simple one, otherwise governmental efforts would have already had proved more successful. Yet, one could argue that, apart from not being sufficiently integrated, policies remain unconvincing in terms of their net benefits.

Policymakers should not lose sight of high-level views on why informality must be addressed, but the calculus supporting formalization efforts should be based on utility. Indeed, the give and take, meaning the benefits and the costs, associated with formality should clearly incentivize informal businesses to go formal. With regards to the latter, costs stem from the monetary and non-monetary demands of formalization, including one-off and on-going charges, fees, and/or duties and obligations that formal businesses are responsible for. And with regards to the former, the benefits build on the explicit advantages, those critically instrumental, not of abstract nature, that businesses gain from formalization, as well as the opportunity costs of remaining informal which can be assessed as the implicit advantages of being part of the formal sector.

For businesses, formalization increases access to productivity enhancers. Formal businesses can openly engage all sorts of business counterparts, from suppliers to customers, in particular those, such as larger organizations or more demanding clients, that would not engage with an informal (business) partner. Being registered increases the opportunities for market recognition and access to business services, from simple transactions such as opening a bank account or applying for credit to others more complex like beholding property or upholding contractual rights. Finally, by becoming part of the formal economy, businesses and their owners are also relieved of potential risks arising out of informality, notably, tax and social security penalties, corruption and intimidation.

For governments, formalization contributes towards stronger institutional pillars. Formal enterprises benefit from protection and access to arbiters of last recourse in business-to-business transactions. As well, employment and labour markets are better protected through the formal sector, not only by providing arbiters of last recourse in labour disputes, but also by protecting workers through health, pension, and unemployment insurance. Formalized entrepreneurs, and not only workers, also gain from the government having access to more and better data on businesses, because of the importance of having business statistics as the basis for sound entrepreneurship, and supportive public policies. Finally, consumers are beneficiaries of greater business formality through increased consumer protection and, overall, from greater (formal) market sophistication.

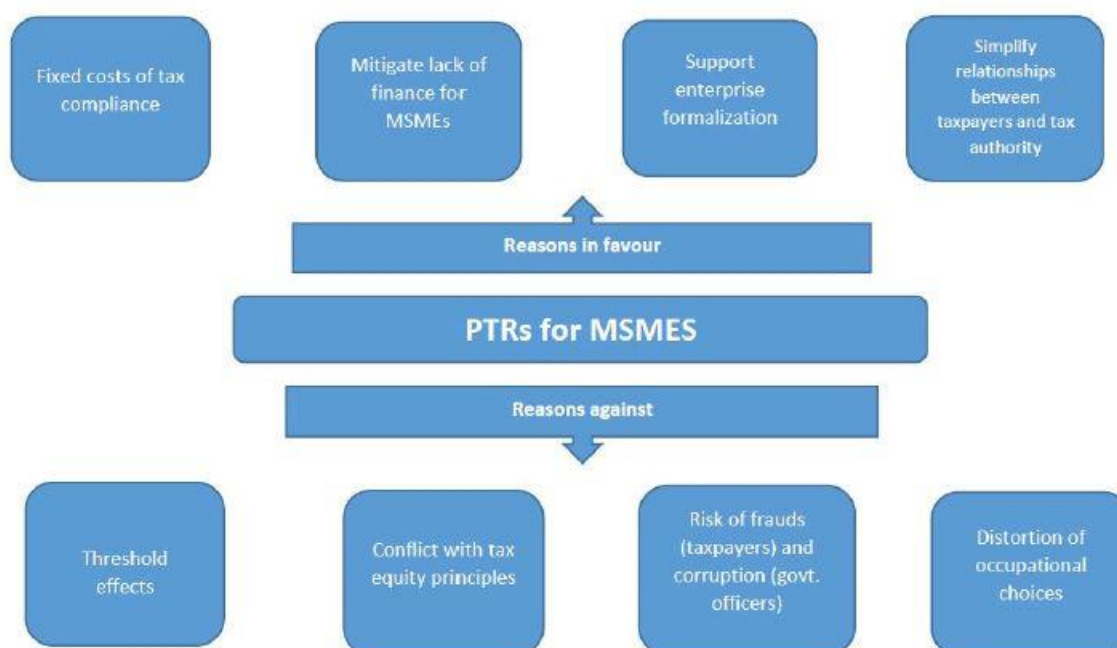
► The typology of governmental (formalization) interventions

Facilitating a gateway between the informal and formal economy is key. According to the World Bank (2022), in its novel approach on measuring the business enabling environment, there are three elements that should be observed when assessing the regulatory framework: the quality of regulations for business entry; the availability of public services; and the efficiency of business entry in practice. These elements are closely related to the practical features built into the tools that allow businesses to register. Featured examples include the ease of use of business registries, and the time to complete registration, as well as the interoperability of those registries with additional datasets managed by public-and-private sector institutions (for example, tax and social security authorities, statistical offices, asset/credit registries, and digital identity databanks, among others).

Providing safe passage to existing informal businesses that are willing to formalize could be considered. For many existing businesses in the informal sector, the decision to formalize may not be equivalent to that same decision undertaken by a newly created business start-up. Legacy concerns at existing (informal) businesses may indeed blur and deter the calculus involved in formalization when no clarity is provided about the consequences of past (business) misdemeanours upon entering the open playing field. Existing rules must be upheld whenever applicable. Yet, one could argue that downplaying the past minor violations of businesses, except for gross abuses of the law, and focusing on business practices once they are registered in the formal economy might prove reasonable, sensible, and inductive of the desired goal.

Governmental interventions aimed at formalization usually include carrots and sticks. In low-and-middle income countries, the typology consists in the following instruments: information interventions; simplification and registration interventions; tax incentives and social security payments reductions; financial incentives; and labour inspections and enforcement interventions (Jesse and Kluve 2019). In these low-and-middle income countries, where the level of economic informality tends to be higher, simplification and registration interventions have understandably proven more frequent. Yet, tax incentives and social security payment reductions are the most impactful in reducing informality. Labour inspections are also highly effective although the least frequently used instrument utilized by government officials.

► **Figure 2: Reasons in favour and against preferential tax regimes (PTRs) for MSMEs**



Source: Marchese (2021).

Public-private partnerships towards making formalization strategies operational should not be disregarded.

In low-income countries especially, where the institutional capacity to provide for effective formalization of the informal sector is often lacking, relying on private sector organizations to collect data and assist in policy delivery could be a good compromise solution. Policy development can also be assisted by private sector organizations, as well as through social dialogue. Employer and worker associations are knowledgeable about the micro dynamics of the business sector, and of its market practices, in addition to having the capability of reaching out to vast numbers of businesses. Thus, they can contribute not only to the design of programmes, but also towards a greater uptake of those that are potentially eligible.

Governmental interventions are increasingly based on e-formality, delivered through digital technologies.

Seemingly, there is growing evidence of a link between e-formality and the transition into the formal economy (Williams 2023). Digital technologies make registration simpler, more functional, and allow for increased coordination between governmental entities, reducing administrative bottlenecks and overlaps. Formalization procedures typically involve a few different frontline ministries (for example, ministry of finance, social security, economy, labour, agriculture, interior, migration, and/or others), thus, intra- and inter-governmental coordination is critical. E-formality allows for the embedding of different policies into a full formalization policy plate, via a single gateway, preferably digital, without which registration only would not suffice.

► Simplified business registration and enforcement

Governments use simplified registration regimes, tailored to MSEs, first and foremost to gain direct access to primary data on business demographics. Enticing unregistered businesses with a simplified regime then creates the opportunity for delivering the carrots and sticks mentioned above, including educating MSEs on proper management routines and disciplining misbehaviour. Low- and middle-income countries frequently use simplified regimes that, in addition to facilitating the registration process itself, employ the use of taxing, reporting, and accounting exemptions, or other preferential regimes to incentivize MSE registration (related to cost, tax, social security, market links, etc). These tailored procedures are usually named under specific designations, such as Morocco's 'auto-entrepreneur', the 'statut d'entrepreneur' adopted in member countries of OHADA in Africa (for example, Benin), and India's 'Udyam' regime (Annex, Boxes 1-3).

Simplification begins with procedural mapping. According to the ILO (2021b), bureaucratic requests must be streamlined, and this starts by mapping out information requirements and the procedural sequence towards completing registration. One-stop shops, first physical and now essentially virtual, have been the main option in countries willing to increase government coordination and to reduce time to market for formal businesses. Chile, Colombia, and (once again) Benin – which in Africa has conducted several highly regarded e-formalization policies (see ILO 2021b and ILO 2021f) – exhibit interesting, tailored case-studies (Annex, Boxes 4-6). In the case of Colombia, its virtual VUE (Ventanilla Única Empresarial) platform aims at tackling four different dimensions of informality in one place: business and property registration, tax payments, one-off and on-going regulatory non-tax obligations, and product certification if applicable.

Digital technology is increasingly regarded as boosting formalization success rates. Williams (2023), based on a broad analysis of available literature, observes a negative correlation between (reduced) informality and the take-up (or increase of use) of e-formality options. Interestingly, existing evidence also suggests that there is no relationship between the take-up of e-formality and the level of development of individual countries (Annex, Box 7). While there are technical obstacles working against the implementation of digital public services, such as broadband infrastructure and internet use by the general population, e-formality advances are seemingly more related to the political will involved in advancing such innovations in the public sector. Yet technology alone will not boost formalization if the net benefits associated with it are unconvincing.

Despite the focus on net benefits, formalization policies require public investment and institutional obligations. Enforcement is also required, and labour inspections are essential in guaranteeing that the grand bargain implicit in formalization, between policymakers providing the incentives and MSEs assuming legal obligations, is kept intact. However, as discussed above, labour inspections are the least used governmental interventions within existing options. Inspections are invasive and, from an administrative point of view, they are frequently not efficient either. Yet technology has made possible new ways not only to conduct labour inspections, but also to keep track of them. Already, countries such as Sri Lanka (Annex, Box 8) and Bangladesh are using digital applications to that end. In addition, other countries such as Hungary (Annex, Box 9) and Bulgaria as well have developed easy-to-use systems to account for seasonal and temporary labourers.

Policymakers can improve the case for formalization by eliminating administrative frictions and gaps, adopting innovations as well. E-business registries should be complemented by e-employment and e-tax registries, e-invoicing platforms and digital standards for property and credit registries linking the public and private sectors. Estonia provides for all that and much more (Annex, Boxes 10-11). Recent innovations in its e-government include the e-Residency status, under which non-Estonians can apply for residence and register businesses without the need to relocate, and so-called Entrepreneurial Accounts, which are private bank accounts linked with the tax authority, tailored to VAT-exempt own-account workers. Pre-filled forms in digital public services, as part of a novel 'non-stop shop' model whereby businesses just validate pre-filled data, are also increasingly used in Estonia, especially in tax returns, but also in the Nordics as well as in incorporation documents in the Philippines.

Governments should also consider the financial liabilities involved in MSE business structures. This is a very frequent concern among MSEs because of the typical unlimited liability setup under which many of these businesses are usually established, incentivising the co-mingling of personal and business assets, sometimes with devastating consequences for entrepreneurs and their families. Micro entrepreneurs tend to be personally liable for all debts (including financial, commercial, social security and tax liabilities) arising from their business endeavours. In the face of that, some regimes, such as Morocco's "auto entrepreneur" (Annex, Box 1), attempt to introduce limited liability. Yet perhaps more pragmatically, an alternative could be to discharge personal debts from business dealings, after a pre-determined number of years (for example, 3 years), following debt restructurings (as proposed in the European Union via EU directive 2019/1023).

Simplification represents not only addressing the concerns of entrepreneurs, but also being flexible to collective administrative alternatives when the institutional capacity is not available. Collective registration agreements, whereby non-governmental organizations, such as employer associations, enable the option of indirect registration of MSEs, and indirect social security coverage of their workers, are an example. Another example is associational taxation, whereby governments are assisted by private sector organizations in the collection of taxes, giving greater voice to non-governmental stakeholders in both policy design and policy implementation (ILO, 2021c). In the case of the former, Costa Rica has long had such a regime, dedicated to own-account workers in the agricultural sector. In the latter case, Ghana has some experience, although tax issues are perhaps better managed by government officials only.

► Preferential taxation, social security coverage and other incentives

Tax incentives and social security are a very common feature of formalization policies worldwide. These have been implemented mostly in Latin America, but also across Asia and Africa, and in Europe as well. Tax incentives usually assume the form of presumptive taxation, whereby MSEs are taxed based on some specific proxy of economic activity such as turnover, size of premises, and electricity consumption. Turnover-based, presumptive taxes are a popular choice of option in many countries, applying a tax rate on top-line business revenues – as opposed to bottom-line net profits – or a fixed fee payment. Turnover taxes are usually accompanied by some degree of book-keeping, subject to maximum revenue thresholds, and they may integrate the payment of other taxes, such as value-added taxes (VAT), as well as social contributions. Variations of turnover taxes can be found in Argentina, Uruguay, Colombia, South Africa, Georgia (Annex, Boxes 12-16), and many others.

Fixed fees and single payments, covering tax and social contributions, constitute best-practice entry-level mechanisms in formalization policies. They entice microbusinesses, including own-account workers, by offering the possibility of a single tax payment, which tend to reflect policymakers' priority towards registration rather than maximising tax revenue collection. Brazil's MEI regime has attracted the interest of millions of Brazilians since its inception (Annex, Box 17). It is aimed at micro entrepreneurs employing up to one employee and is based on a single low tax payment, exempting eligible businesses from income taxes and replaces state and municipal-level taxes as well as social security contributions. Being able to access welfare coverage has been highlighted as a major advantage of such regimes, in addition to the other benefits associated with formalization.

Blanket exemptions for income tax, under a low business revenues threshold, constitute yet another entry-level mechanism, and may also exhibit limitations. Georgia and Armenia (Annex, Boxes 18-19) in Eastern Europe both offer such exemptions, though in the former the regime is only available for sole entrepreneurs without hired labour, whereas in the latter it is available for entrepreneurs with hired labour. In Armenia's case, by not limiting the regime to businesses without hired labour, registration gains have been impressive. These regimes typically do not require formal bookkeeping, being based on self-reporting, although the use of cash registers may be required. The activities allowed under these regimes (including fixed fee payments) are usually restricted to government-approved lists, focusing on professional services and proximity businesses.

Threshold determination is a critical design feature of presumptive (income) tax policy. According to the IMF (2022), in Latin America where presumptive taxation is widespread, the top threshold of fixed fee payment regimes, above which microbusinesses graduate to turnover tax regimes, was on average 4.2 times GDP per capita, and 54.5 times GDP per capita in the case of turnover taxes (based on 2019 data). The former is applicable to natural persons, sole proprietorships, and micro businesses, and the latter to relatively larger SMEs. Importantly as well, minimum VAT-registration thresholds (i.e., above which businesses must register for VAT compliance) should also be aligned with (top) turnover thresholds, which is often not the case, creating further imbalances in the design of preferential taxation regimes.

For turnover taxes, from a design perspective, defining tax rates applicable to specific thresholds is also key. Latin America, again, showcases the extreme variation of turnover tax rates, with these ranging from 0.3 per cent to 33.0 per cent (IMF 2022), given varying tax bases. Elsewhere, practices differ. In Georgia the turnover tax exhibits two rates, whereas in Armenia there are multiple rates within that tax structure (ILO 2021d and ILO 2021e). Balancing these technical issues is not simple, and presumptive taxation regimes have been shown to produce so-called threshold effects. In other words, some businesses remain just below applicable thresholds, justly or artificially, and do not graduate into more general, regular tax regimes. This is why in some countries, such as Indonesia or Mexico (Annex, Boxes 20-21), reduced corporate income tax (CIT) rates also exist.

Low and reduced tax rates for small businesses, or preferential CIT rates, are critical and can range from simple rate discounts to more elaborate reduction schemes. This latter case indeed applies to Mexico, which

applies discounts over ten-year periods not only on CIT, but also on VAT and social security contributions. Yet, while tax incentives are regarded as highly impactful in reducing economic informality, expectations must be realistic. Tax policy is not a silver bullet. Offering tax incentives can certainly alleviate the financial costs that are associated with formalization and, importantly, they increase the after-tax return on invested capital. However, these advantages, especially the latter, are best captured by those businesses that grow into more productive enterprises and eventually graduate into the general CIT regime.

Formalization policy should incentivize businesses to gradually evolve from the initial stages of mere MSE registration to the later, more mature stages of corporate development. This is why a continuum of policies, of which simplified registration and preferential taxation are just pieces in an overall puzzle, is thus needed. Governments should develop policies to expand market opportunities and strengthen business linkages not only by providing incentives aimed at increasing collaboration between private sector businesses (for example, through joint ventures) but also enhancing public-private collaboration, export promotion, foreign domestic investment attraction, supplier linkage promotion and supplier clubs, matching platforms for business succession, access to credit guarantee schemes, access to training, public procurement, whistle blower platforms, and other measures within the kit of MSME public policy.

► Lessons learned from international examples for HHBs in Viet Nam

The use of digital technology has emerged as a dominant theme throughout this report. From registration procedures to tax, labour and other issues, ignoring digital developments conveys the risk of massive judgement errors by policymakers. As highlighted above, the adoption of e-formality is less related to the level of development of individual countries than it is to the political will of national policymakers. E-formality adopters include low- and middle-income countries such as Bangladesh, Benin, India and Sri Lanka, among others, and not only e-government champion Estonia or high-income countries in Nordic Europe. Given the examples provided here, no serious attempt at addressing economic informality can be made without the use of e-business and e-employment registers, as well as related applications (for example, electronic case management of labour inspections) or e-portals for tax and social contributions payments.

Access to social insurance and, in general, to welfare programmes, embedded in simplified registration options, as well as in preferential taxation schemes, is highly regarded. This is seemingly more appealing in low- and middle-income countries, where large swathes of the workforce remain employed in informal jobs and, frequently, below or near poverty line levels. Providing some degree of social protection (through unemployment, health, and/or pension benefits), even if initially subsidized in part by taxpayers through low or discounted rates, could be the key incentive to bring more people into the formal sector, laying ground for the social elevator to make its way upward. In any case, attention should also be dedicated to violations of simplified regime rules, notably those related to threshold effects that arise in labour (for example, underreporting hired labour by categorising employees as independent own-account workers) or in taxation (such as underreporting of revenues).

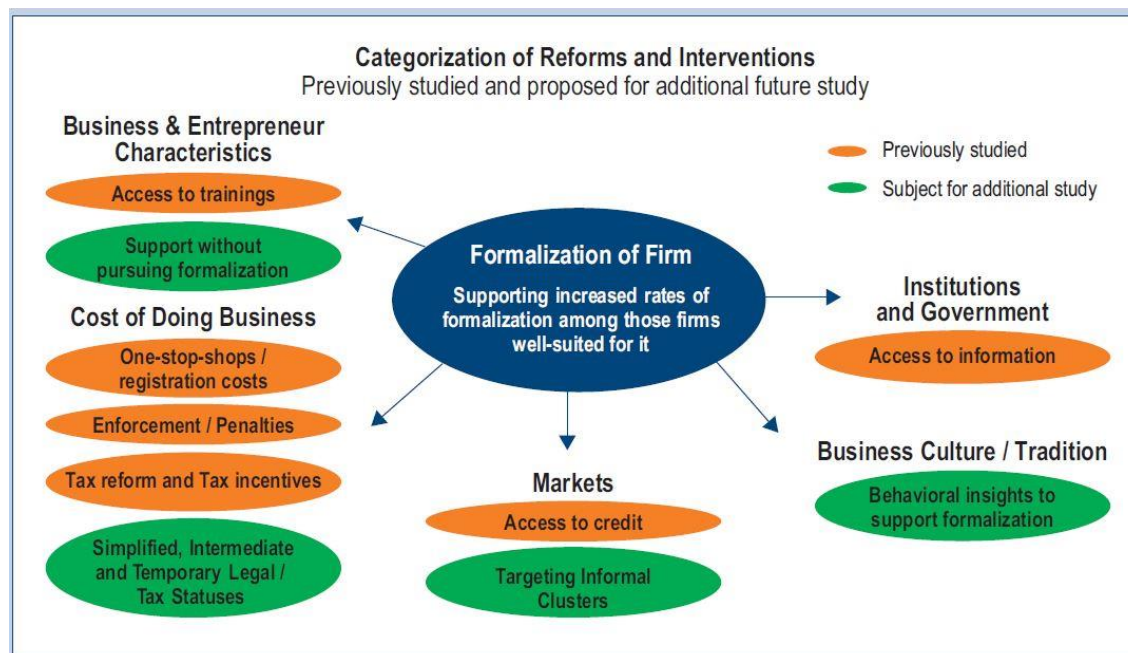
Preferential taxation tailored to MSMEs is salient in formalization strategies. The gamut of available regimes around the world is impressive. But the risk in preferential taxation resides in having too many tax regimes, leading MSEs into confusion. Establishing clear exemptions and defining reasonable turnover thresholds are key. The former need not be subject for tax specialists only, and the latter can be solved by using a multiple of GDP per capita, depending on whether it is applied to a fixed fee payment modulation of preferential taxes, aimed at the smallest lot of MSEs, or to a turnover tax proper, aimed at larger SMEs. Additional design concerns pertain to the alignment of the minimum VAT-registration threshold and the top turnover tax threshold, which should be set equal, and defining standard preferential tax rates, which from a technical perspective in the case of a turnover tax should be slightly more onerous at the upper threshold level of the preferential tax regime than the general CIT rate of the corporate tax regime, to avoid threshold effects (Wei and Wen 2019).

The issue of financial liability remains, however, troubling. Only recently have policymakers, mostly in high-income countries in Europe and North America, dedicated increased attention to the financial fragility of MSEs, and the uneven playing field they frequently encounter in their day-to-day activities. Whilst some incentives can be created to ameliorate the tax treatment of internal equity (for example, in Estonia reinvested earnings are CIT-exempt), or access to external finance, more work could be done in de-limiting the liabilities incurred by micro entrepreneurs who are subject to personal, unlimited liability in their business dealings. Thus, aiming for limited liability legal structures, the kind that incentivize entrepreneurs and shareholders in high-income economies to take risk, while reasonable in theory, can backfire into less access to credit. If banks are not restrained in their collateral demands, and furthermore in their negotiating stance under debt restructurings, circumventing a (limited liability) legal statute for MSEs is easy.

Financial literacy and inclusion, and the use of e-payments, is increasingly under the spotlight around the world, not least in Viet Nam. The country's political leadership has signalled its desire to move towards a cashless society, and recent pilot programmes have attempted at promoting e-payment services for ethnic minorities in rural and remote areas (World Bank 2021). Formalization would benefit from a move towards a cashless society. Advances in that direction increase the traceability of informal transactions, as well as the fine-tuning of

presumptive-based tax regimes and of enforcement inspections of all kinds. Widespread use of e-payments and enhanced bank accounts (for example, Estonia's Entrepreneurship Accounts) provides governments with structured and unstructured data, which in turn can be used to feed automated algorithms, strengthening the capacity to target informal clusters in a risk-based approach to enforcement action (Williams 2023), currently an area of interest to reformers (Figure 3). Critical to this end are key priorities, including strengthening financial literacy (including for public officials) and banking structure reforms to facilitate e-banking.

► **Figure 3: Re-thinking the approach to informal businesses**



Source: World Bank (2020).

Formalization policy is best implemented when considering multiple dimensions associated with economic informality, while avoiding ostensive harassment of informal businesses. MSEs, most of all, must be carefully nurtured into the system, offering them functionality embedded in simple and ideally automated, frictionless registration procedures that maximize immediate utility within politically acceptable boundaries. Some countries, including low- and middle-income countries, seemingly achieve this on high marks, notwithstanding the professional scepticism that is always recommendable. Benin's GUFE, Colombia's VUE and India's Udyam illustrate simplified registration frameworks that attempt at mapping out initial requirements, delivering tangible benefits to businesses such as the capacity to register property, obtain product certifications, and open a bank account.

This report has developed the theme of simplified registration regimes and MSE-focused formalization frameworks, to inform policymakers in Viet Nam of existing options in different jurisdictions. The concept of a HHB is typical of Viet Nam, and analogues cases do not abound. The closest to Vietnamese HHBs is perhaps India's Hindu Undivided Family (HUF) type of business (Annex, Box 22), in which the business is collectively registered and owned by the family, although the managing role, in representation of the family unit, is exercised by the family's eldest family member (the so-called Karta). In Viet Nam, however, HHBs can also be established by individuals. The HUF regime, based on caste and suffering from a potentially complex ownership structure that greatly complicates dissolution and exit, plus the troublesome conjunct liability shared among family members, despite the dominant role played by the family's leading member, is uninspiring (contrary to India's very inspiring e-government drive).

The Vietnamese HHB statute is disturbed by its unconventional eligibility criteria – the concept of a household – and by the fact that both individuals and family members, collectively, can register HHBs. These features are uncharacteristic of micro business regimes found elsewhere in the world, where sole proprietorships or general partnerships, with or without hired labour, are the most common regimes on display, and whereby eligibility thresholds are essentially defined by business revenues (turnover) and/or number of employees. HHBs

are also hurt by the legal conundrums in Viet Nam, where some laws recognize HHBs, while others do not, despite the existence of 1.7 million HHBs already fully operating in the formal economy. Moreover, the nearest alternative to HHBs in Viet Nam, i.e., private enterprise as regulated by the Enterprise Law, is also deemed inappropriate for MSEs. The discussion on a new governmental Decree for HHBs provides an opportunity to address some of the deficiencies in the existing, overall HHB framework by adopting best practices identified in other countries and described in this report.

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► Annex: Country examples and descriptions

► Box 1: Morocco's 'Auto-Entrepreneur' (self-entrepreneur) registration procedure

Target group: Starting entrepreneurs, students, vocational training graduates, unemployed persons and informal operators, including foreigners with an activity in Morocco.

Eligibility: Based on turnover.

Policy description: Auto-entrepreneurs submit formal invoices, declare turnover, pay taxes, comply with relevant sectoral and other regulations and announce the termination, transfer or transformation of the business.

Benefits of this registration: Simplified business creation and termination; Tax reduction: 0.5 per cent of turnover for industrial, commercial or artisanal activities and 1 per cent of turnover for services; Exemption from value added taxes and temporary exemption from business taxes on the rental value of business premises and fixed assets; Exemption from submitting balance sheets to the tax authorities; The possibility of issuing formal invoices; Coverage under the social security scheme from the moment they register as auto-entrepreneur (not yet operational) (...) to benefit from the same legal provisions on health care and pensions as those that apply for other types of entrepreneurs; in case of bankruptcy the property of the entrepreneur will not be at risk.

Source: ILO (2021c).

► Box 2: OHADA's 'statut d'entrepreneur' (individual entrepreneur legal status) regime

Target group: Individual entrepreneurs, natural persons, in member countries of the Organization for the Harmonization of African Business Law (OHADA).

Eligibility: Based on turnover and type of economic activity (within professional, artisanal, and agricultural activities and/or services).

Policy description: The entrepreneur retains his status if the annual turnover generated by his activity for two successive financial years does not exceed the thresholds set in the Uniform Act. (...) The entrepreneur can only begin his activity after receipt of this activity declaration number which he must mention on his invoices, purchase orders, prices and professional documents or correspondence, followed by the indication of the Trade Register and of Crédit Mobilier which received its declaration and the mention "Entrepreneur exempt from registration". (...) The entrepreneur is required to establish, as part of his day-to-day activity, a book chronologically mentioning the origin and amount of his resources, distinguishing cash payments from other methods of payment on the one hand, the destination and the amount of its uses on the other hand. The book must be kept for at least five years.

Benefits of this registration (as implemented in Benin): An experiment conducted by the World Bank in Benin provides convincing evidence that the uptake of the simplified legal status (the statut d'entrepreneur) can be increased if accompanied by 'handholding' services, including: assistance in registering, filling out forms and preparing supporting documents (...); training on accounting, tax obligations and financial literacy and assistance in opening a bank account (...); and mediation services in case of dispute between the firm and the tax administration.

Source: OHADA website (accessed 10 Oct 2023) and ILO (2021c).

► **Box 3: India's Udyam e-registration scheme for MSMEs**

Target group: Micro, small and medium-sized enterprises.

Eligibility: An enterprise shall be classified as a micro, small or medium enterprise on the basis of the following criteria, namely: (i) a micro enterprise, where the investment in plant and machinery or equipment does not exceed one crore rupees and turnover does not exceed five crore rupees; (ii) a small enterprise, where the investment in plant and machinery or equipment does not exceed ten crore rupees and turnover does not exceed fifty crore rupees; and (iii) a medium enterprise, where the investment in plant and machinery or equipment does not exceed fifty crore rupees and turnover does not exceed two hundred and fifty crore rupees.

Policy description: (1) Any person who intends to establish a micro, small or medium enterprise may file Udyam Registration online in the Udyam Registration portal, based on self-declaration with no requirement to upload documents, papers, certificates or proof. (2) On registration, an enterprise (referred to as "Udyam" in the Udyam Registration portal) will be assigned a permanent identity number to be known as "Udyam Registration Number". (3) An e-certificate, namely, "Udyam Registration Certificate" shall be issued on completion of the registration process.

Benefits of this registration: It will be a permanent registration and basic identification number for an enterprise; MSME Registration is paperless and based on self-reporting; there will be no need for renewal of registration; any number of activities including manufacturing or service or both may be specified or added in one registration. Along with the Udyam Registration, Enterprises may register themselves on GeM (Government ePortal (a portal to address issues relating to delay in payments) and simultaneously MSMEs themselves can also onboard on TReDS Platform (the invoices of receivables are traded on this platform) through three available platforms (www.invoicemart.com, www.m1xchange.com, www.rxil.in); the Udyam Registration may also help MSMEs in availing the benefits of Schemes of Ministry of MSMEs such as Credit Guarantee Scheme, Public Procurement Policy, additional edge in Government Tenders & Protection against delayed payments; becomes eligible for priority sector lending from Banks.

Source: Office of Development Commissioner, Ministry of Micro, Small and Medium Enterprises (Feb. 2021).

► **Box 4: Chile's 'Empresa en un Día' (One-Day Business registration) procedure**

Target group: Small businesses (under the 'PYME' legal statute).

Eligibility: Based on turnover.

Policy description: Empresa en un Día simplifies enterprise registration through a platform established by the Chilean Ministry of Economy, Development and Tourism. Registration in the Business Registry, the public deed and the publication in the Official Gazette can be completed by filling out a digital form. Since 2013, more than 70 per cent of companies have been created through this digital platform.

Benefits of this registration: The company can start operations immediately upon receipt of the tax identification number assigned by the platform.

Source: ILO (2021b).

► **Box 5: Colombia's 'Ventanilla Unica Empresarial – VUE' (One-Stop Shop) platform**

Target group: Firms in general.

Policy description: VUE is designed to tackle four dimensions of business informality: (i) entry (registration at the Chamber of Commerce), (ii) input (land use and social security affiliation and payments), (iii) product (such as sanitary certificates) and (iv) tax (such as declaration and payment of taxes).

Benefits of this registration: Given its multidimensional nature, the institutional organization for the functioning of VUE requires coordination between several public and private entities and at the national and territorial levels. MINTIC provides the technological guidelines related to the macro-strategy of e-government, and the Ministry of Commerce, Industry and Tourism (MINCIT) is in charge of coordinating VUE. The operation is in the private sector through the Chambers of Commerce and the Association of Chambers of Commerce-Confecámaras. Several additional institutions participate. For input formality, Ministries of Health and Labour play a role in enrolment and payment of social security. For tax formality DIAN is responsible for tax identification. In addition, VUE platform allows the payment of the Department registration tax that depends on the departments tax administration. For product formality, Invima provides services related to compliance with sanitary standards. Finally, at the territorial level, mayors' offices play a role in VUE identifying whether the company is located in the right land use.

Source: Olivera (2022).

► **Box 6: Benin's GUFÉ (Guichet Unique de Formalisation des Entreprises) platform**

Target group: Own-account workers (under the 'entrepreneur' legal statute).

Eligibility: The status of entrepreneur can apply to a natural person who runs a micro or small business carrying out any type of activity.

Policy description: The GUFÉ - Guichet Unique de Formalisation des Entreprises - acts as a one-stop shop and a coordinating institution between the different agencies involved in the registration process. It allows entrepreneurs to register free of charge and in a timely and efficient way and can also deal with all other company statutes (trader, limited liability company, SA, etc.). These are the documents that can be obtained via GUFÉ one-stop shop: Registration number with the Caisse Nationale de Sécurité Sociale (CNSS); Unique Tax Identifier (IFU) from the Direction Générale des Impôts et Domaines (DGID); Certificate of registration in the Trade and Personal Property Credit Register (RCCM); A certificate of registration from the Direction Générale du Travail (DGT).

Benefits of this registration: Free of charge; One-day registration (applies to other status); Tax exemptions after formalization - Businesses that formalize, registered with CGA, and that had not paid taxes before, have a tax exemption for the first year after formalization, in addition to a reduction of 40 per cent in the amount of taxes due for the following 3 years. Open a Business Bank Account; Apply to bank loan; Working with large companies; Chamber of Commerce Registration; Provide invoices to customers for tax purposes.

Source: ILO (2021b).

► **Box 7: Benin's 'monoentreprise.bj' platform**

Target group: Firms in general.

Eligibility: Firms.

Policy description: Web platform that allows entrepreneurs to create their enterprise online, using a computer or an android device. The website is a one-stop shop that allows entrepreneurs to comply with all regulatory requirements on one digital platform. The entrepreneur needs only to present a valid identity document, birth certificate, passport photo and address. Every user must also provide details of the proposed business activities. This initiative was developed by the Government of Benin with financial support from the Kingdom of the Netherlands and technical assistance from the United Nations Conference on Trade Development (UNCTAD). (...) The primary aim of this platform is to facilitate business registration, and support formalization. Entrepreneurs that register through this system do not pay any tax during the first year of their activities, but the tax authorities will thereafter be able to identify them. Monentreprise was launched just before the COVID-19 crisis, and it assisted in the acceleration of enterprise formalization. The number of businesses created between March and June 2020 averaged 2,783. Up to mid-May 2021, already more than 4,000 business had been created per month. One-third of the entrepreneurs that registered through this system were women, half were under 30 and half were based outside Cotonou. Government officials were able to check documents and approve company applications from home, respecting a two-hour time limit. The creation of an online business registration platform was very timely, given the risks associated with in-person interaction during the COVID-19 pandemic.

Source: ILO (2021f).

► **Box 8: Sri Lanka's 'Labour Information System Application (LISA)' enforcement tool m**

Policy description: The mobile app and database system facilitates, simplifies, and strengthens labour inspection and follow-up activities. The app automates the labour inspection process by removing the need for labour inspectors to fill-up multiple paper-based forms and record books during their visits to inspectable units. The data collected during the inspection is stored into the LISA system and the inspectors are able to write an inspection report using the app along with features such as attaching pictures taken on site. The report can be sent to the inspectable units along with a request to remedy problems noted during the inspection. The app has also facilitated effective monitoring and follow-up on non-compliance post-inspection. Additionally, complaints submitted by workers are put on the LISA system and is used by labour inspectors to inquire into them and take required steps.

Benefits of this registration: Upgrading labour inspection through use of technologies that allow for greater transparency, better monitoring and follow-up, and improvement in data collection and processing can boost compliance. It can make labour inspections time and cost effective allowing labour inspectors to cover greater number of establishments.

Source: Bhattarai (2018).

► **Box 9: Hungary's 'Simplified Employment in the Agricultural Sector' registration procedure**

Policy description: The 2010 Simplified Employment Act introduced a simple electronic registration which records the exact date and time of the start of the employment relationship, making it easier to carry out temporary (casual and seasonal) employment on a declared basis and conduct inspections. By facilitating employment notifications, reports and payments through the use of an electronic notification tool, the Simplified Employment Act aims to increase legal casual employment in any sector as well as seasonal employment in agriculture and tourism, while making it easier to conduct labour inspections.

Benefits of this registration: A mobile application tool was introduced in 2017. Employers can now register the start of the simplified work relationship via the app or via the client gate system; A written contract is not required, unless an employer or the employee wishes to have one. The contract form provided as an appendix to the law can be used as a template; While a worker can simultaneously have a simplified employment relationship with more than one employer, an employer cannot employ the same worker for seasonal employment using simplified employment for more than 120 days in a given year; Working time can vary across days e.g. four hours in one day, three in another. The employer can schedule Sundays and public holidays. Sunday work does not necessitate the payment of the statutory Sunday wage supplement, but the public holiday wage supplement must be paid. The simplified work rules thus permit flexibility in terms of seasonal and agricultural work while still protecting employees and preventing undeclared work; Employers cannot use the system if they have unpaid/overdue taxes of over EUR 913; Registered jobseekers do not need to notify public employment services about the simplified employment relationship, thus retaining their jobseeker status, without interruption, for the duration of the relationship.

Source: European Commission (2019).

► **Box 10: Estonia's e-government direct and indirect policies for business formalization**

Policy description #1 ("e-Tax"): First introduced in 2000, e-Tax facilitates the online declaration of tax (...) In addition, in 2003, the tax return became pre-filled based on data that had been collected. Therefore, and unsurprisingly, it takes an average of three minutes to complete one's tax declaration online. Not only used for individual income tax claims, companies themselves can also declare income tax, social tax, unemployment insurance and pension fund contributions through e-Tax. A significant incentive to convince taxpayers to file their taxes online was linked to the quick refund of money if one had overpaid. (...) the electronic filing of one's tax declarations meant a refund waiting period of five days. By 2019, approximately 98 per cent of tax declarations are completed online and use the digital identification method (...)

Policy description #2 ("e-Register of Employment"): Whether working in a company or as self-employed (covered later below), access to social protection is contingent on registration. To further support the registration of employees, amendments in 2014 to the Estonian Taxation Act made it mandatory of employers to register their workers on an employer's register. The Estonian Tax and Customs Board (ETCB) established this as an electronic register. It meant that employers could register their new employees online in a 'one-stop shop' which also inputted the information to the Estonian Health Insurance Fund and the Unemployment Insurance Fund, thereby automatically enrolling the worker in social protection.

Policy description #3 ("e-Business Register"): The establishment in 2007 of the e-Business Register makes registering a business online a simple and efficient process, and can be done without the usage of a notary. For the legal framework of the business, once logged into the portal, a business owner can access different legal templates with articles of association which the business owner can use and assemble as is best fit to his/her needs. Again, because these are legally coherent and relevant, there is no need for a notary nor lawyer to help set up the business. The e-Business Register also allows the company to update its own data, file annual reports, and make queries about other companies. As of 2019, 98 per cent of companies were established online.

Source: Divald (2021).

► **Box 11: Estonia's e-government recent innovations in business formalization**

Policy description #1 ("e-Residency"): Another important development was in 2014 with the distribution of the first e-Residency card. The concept of e-Residency began in 2008 when Estonia opened up its e-services to non-Estonian citizens. The system was formalized in 2014 where anyone in the world could apply. Upon successful application, the e-Resident was given an Estonian e-ID and access to Estonia's digital business environment. The e-Resident could perform the following online: digitally sign documents; register a company; open and access a bank account; and declare taxes. The policy was aimed at promoting Estonia's image as a leading provider in online services and to advance its economy. As of 2020, there were more than 70,000 Estonian e-Residents, establishing over 13,000 companies and from over 160 countries.

Policy description #2 ("Entrepreneurial Account"): A recent innovation which arose in January 2019 was the creation of an entrepreneurial account, or business account, in collaboration with an Estonian bank, LHV. While LHV is the bank that offers the service, it is open to other banks as well. The entrepreneurial account is an ideal system for private person-to-person services such as personal cleaners, lawn mowers, nannies, etc. and a simple solution to decrease the informal economy. When the entrepreneur becomes a business account owner, the bank automatically transfers his/her information to the tax authorities and calculates the amount of tax to be paid. All this is done free of charge. (...) The business account owner can also receive health insurance as long as the user contributes the minimum amount of social tax (as of early 2021, the minimum social tax obligation was 192.72 euros). As of October 2020, over 3,000 new entrepreneurial accounts have been created with more than 1 million euros of payments to the accounts. Such measures make it easy to comply with tax rules and thereby also reduces the informal economy. If the business account owner earns above 40,000, they must either register as a sole proprietor (paying social tax and therefore being covered by social protection) or as a business as legal person.

Source: Divald (2021).

► **Box 12: Argentina's 'Monotributo' (single tax) regime**

Target group: Own-account workers and microbusinesses (with or without hired labour).

Eligibility: Based on turnover.

Policy description: The "Monotributo" (Single Tax) is a presumptive tax regime based on turnover sales, which was originally established in 1998. Enrolment is voluntary, relying on regular self-assessment, and the regime is aimed at own-account workers and microbusinesses (with or without hired labour) operating in multiple economic activities including the agricultural sector. The single tax payment replaces (profit) income tax and VAT, and in addition also pays for social security and health insurance. Restrictions are placed on the size of premises used for commercial activity, annual electricity consumption, and annual rental expenses to control against fraud. The regime's structure consists of eight general categories of annual turnover. From category A, businesses earning up to ARS 1.4 million per year, through category H, for businesses earning more than ARS 11.4 million.

Note: Updated for applicable turnover thresholds as of Oct. 2023.

Source: ILO (2021e).

► **Box 13: Uruguay's 'Monotributo's (single tax) regimes**

Target group: Own-account workers, partnerships, and micro and small enterprises (depending on the regime).

Eligibility: Based on turnover and number of employees/partners (depending on the regime).

Policy description #1 ("Monotributo General"): The general regime of Monotributo (hereinafter "Monotributo General"), established in 2001 by Law 17.296 and extended in 2006 by Law 18.083, is a simplified regime that combines social security contributions and income tax in a single payment that is collected by the BPS. It is specifically aimed at self-employed workers, understood as personal companies with no more than one employee (including those in which the spouse/common-law partner collaborates), companies with up to two partners and without employees, and family businesses with up to three partners and without employees.

Policy description #2 ("Monotributo Social"): In December 2011, Law 18,874 established the Social Monotributo regime, under the supervision of the Ministry of Social Development (MIDES). The regime was updated in 2015, 2018 and 2020. This type of monotax is aimed at a more targeted target population: members of households that are below the poverty line (set by the INE) or in a situation of socioeconomic vulnerability according to the conditions defined by the BPS in accordance with Decree 322/008. (...) The objective is similar to that of the Monotributo General: to incorporate this population into the formal economy and social security protections through the payment of lower contributions and providing payment facilities in the first years after registration. The types of registrants accepted are similar to those of the General Monotributo regime, with some differences: in particular that they cannot have employees, and that after two months without paying the contributions the Monotributo is frozen and does not generate interest. The worker, paying those months, can reactivate his registration.

Source: Aguiar et. al (2023).

► **Box 14: Colombia's 'SIMPLE' (Simplified tax regime) regime**

Target group: Sole proprietorships (and firms in general)

Eligibility: Based on turnover.

Policy description: SIMPLE unifies payment of income, consumption and industry and commerce taxes, through an annual declaration, and any sole proprietorship company or a firm with income inferior to 100.000 Taxable Value Unit (a TVU in 2021 was COP 36.000 or US\$9) can enroll in this tax regime. They must pay in addition social security and parafiscal contributions, which are not included in SIMPLE. This tax regime includes different tax rates, depending on the sector (minimarkets, hair salon, retail, technical and mechanical services, food and beverage, etc.) and on income ranges [Ranges are below 6.000 VTU, above 6.000 and below 15.000 VTU, above 15.000 and below 30.000 VTU, above 30.000 and 100.000 VTU]. Enrolling to the SIMPLE Regime is online, and getting the tax ID (RUT – Registro Unico Tributario - RUT) can be done online too. These are two e-formality policies. Both processes, SIMPLE and tax ID were designed independently and online and then connected. In concordance with e-formalization, any firm in the SIMPLE regime must issue e-receipts. In sum, SIMPLE is a new tax regime that simplifies tax procedures for small firms and that uses online platforms, and hence can be considered an e-formalization policy.

Source: ILO (2022).

► **Box 15: South Africa's Turnover Tax regime**

Target group: Individuals (sole proprietors), Partnerships, Close corporations, Companies, and Co-operatives.

Eligibility: based on turnover.

Policy description: The turnover tax system replaces Income Tax, VAT, Provisional Tax, Capital Gains Tax and Dividends Tax for micro businesses with a qualifying annual turnover of R 1 million or less. A micro business that is registered for turnover tax can, however, elect to remain in the VAT system. (...) There are three payment dates: 1st payment is in the middle of the tax year on the last business day of August (...) 2nd payment is at the end of the tax year on the last business day of February (...) Final payment is after the annual Turnover Tax Return is submitted and processed. The submission of turnover tax returns is in line with the submission of the annual income tax returns, between 1 July and 31 January of the following year.

Turnover (R)	Rate of tax (R)
0 – 335 000	0%
335 001 – 500 000	1% of each R1 above 335 000
500 001 – 750 000	1 650 + 2% of the amount above 500 000
750 001 and above	6 650 + 3% of the amount above 750 000

A big advantage of turnover tax is the reduced record-keeping requirements. The following records must be kept: 1) Records of all amounts received; 2) Records of dividends declared; 3) A list of each asset with a cost price of more than R10,000 at the end of the year of assessment as well as of liabilities exceeding R10,000. To take account of the typical expenses incurred by a micro business and to eliminate the need for detailed recordkeeping of deductible tax expenses, the turnover tax rates are significantly lower than the tax rates under the standard tax system.

Source: South African Revenue Service (accessed 10 Oct. 2023).

► **Box 16: Georgia's turnover tax regime**

Target group: Own-account workers and micro businesses.

Eligibility: Based on turnover.

Policy description: This regime caters to individual entrepreneurs employing hired labour, generating larger sales, and frequently already registered as VAT payers. Under this preferential regime, a turnover tax, rather than a profit tax, applies on gross incomes received from sales. Other incomes, such as financial streams and gains associated with capital transactions, are not taxed as turnover, but as incomes subject to income tax. Salaries paid to hired labour are subject to withholding payments, except for hired workers with annual salaries up to GEL 6 000 employed by small businesses with annual sales no greater than GEL 50 000. Cumulative monthly turnover (sales) up to GEL 500 000 is taxed at a rate of 1 per cent, whereas excess sales above GEL 500 000 are taxed at 3 per cent. Payments are made monthly and must be accompanied by a (monthly) tax return.

Source: ILO (2021d).

► **Box 17: Brazil's 'Micro Empreendedor Individual' (MEI) regime**

Target group: Own-account workers and micro entrepreneurs employing no more than one employee.

Eligibility: Based on turnover and subject to a maximum of one employee (in addition to the entrepreneur).

Policy description: MEI entrepreneurs cannot exceed BRL 81,000 in annual gross revenues, cannot employ more than one person, cannot be a partner, administrator or owner of another business, and must operate in a sector covered by the regime (over 400 activities mostly in the area of personal services). MEI features the following preferential conditions: i) social security contributions are set at 5 per cent of the minimum salary; ii) a fixed monthly payment is paid to cover a state and municipal tax, i.e. ICMS and ISS; iii) if the business has an employee, the microentrepreneur pays 3 per cent of the employee's remuneration into the social security system, while 8 per cent is deducted from the employee's salary into the Guarantee Fund of Work Time (Fundo de Garantia do Tempo de Serviço, FGTS); iv) businesses are exempt from income taxation and other federal taxes; v) taxes are paid electronically once a year. The whole MEI registration process is also conducted through an easy-to-use online portal.

Source: OECD (2020).

► **Box 18: Georgia's microbusiness tax exemption**

Target group: Own-account workers and micro businesses.

Eligibility: Based on turnover.

Policy description: Individual entrepreneurs in Georgia can establish microbusinesses exempt from income taxes. An individual entrepreneur, under the tax code, is a natural person engaged in business activities. This business status is the most common in Georgia. In 2020, among active (business) entities, 60 per cent were registered as individual entrepreneurs. This status follows not only the tax code, but also Georgia's Law on Entrepreneurs. It requires that individuals must register as entrepreneurs at the Entrepreneurial Registry, operated under the Ministry of Justice, before engaging in for-profit economic endeavours. (...) Having no employees is a first condition. A second condition is having a gross receivable income of no more than GEL 30,000 per year. Georgian microbusinesses are entirely exempt from income tax, and they are also not subject to any accounting requirements. However, they are required to keep records of business transactions (...), and a tax return must be filed annually as well. Microbusinesses cease as such under three scenarios: administrative revocation of the status; inventory stocks valued at more than GEL 45,000; or upon VAT registration.

Source: ILO (2021d).

► **Box 19: Armenia's microbusiness tax exemption**

Target group: Own-account workers and micro businesses.

Eligibility: Based on turnover.

Policy description: Starting from 2020, a new micro entrepreneurship taxation regime has been introduced (...), whereby micro businesses engaged in specific activities, outlined by governmental decree, and generating sales revenues below AMD 24 million, are exempt from the turnover and profit taxes. (...) This preferential tax regime generally excludes trading activities (i.e., defined in the tax code as "purchase and sale" types), while also limiting access for services-based activities. As regards tax payments, the micro regime requires eligible businesses to withhold and pay AMD 5.000 monthly per hired employee. (...) The regime is not available to businesses registered for VAT (in the case of small taxpayers that voluntarily register for VAT) nor to those found in violation of cash register rules more than three times during a calendar year. Continued eligibility for the regime depends on the level of reported sales revenues, which must be communicated to tax authorities by February 1st of every new year with reference to the previous year's business activities. Access to the regime is not limited to businesses of one. Micro businesses operating with paid employees, other than the leading entrepreneur, are also eligible. Since the inception of this framework, the number of registered micro entities has surged.

Source: ILO (2021e).

► **Box 20: Indonesia 'Small Company (Tax) Discount' regime**

Target group: Micro and small enterprises.

Eligibility: Based on turnover.

Policy description: Small enterprises (i.e. corporate taxpayers with an annual turnover of not more than 50 billion rupiah [IDR]) are entitled to a 50 per cent tax discount of the standard rate, which is imposed proportionally on taxable income on the part of gross turnover up to IDR 4.8 billion. Certain enterprises with gross turnover of not more than IDR 4.8 billion are subject to final income tax at 0.5 per cent of turnover.

Source: PwC World Tax Summaries (accessed 10 Oct. 2023).

► **Box 21: Mexico's 'Regimen de Incorporacion Fiscal' (RIF) regime**

Target group: Own-account workers and small businesses (with or without hired labour).

Eligibility: Based on turnover and educational background of employees.

Policy description: For small business activities which do not require the hiring of people with college degree and whose annual income does not exceed MXN 2 million. The main tax advantage of RIF is a 10-year discount on the income tax liability, with the generosity of the rebate that decreases over time, from 100% in the first year of participation in the programme to 10% in the 10th year. Furthermore, the income tax is calculated on a cash-flow basis. RIF participants also benefit from preferential VAT, based on a simplified schedule of tax rates that vary by economic activity, type of product and company turnover. The total VAT liability is reduced based on the same discount rates that apply to the income tax. Social security contributions are also progressively discounted, but at half the rate of the income tax and the VAT.

Reduction in tax liability	Year									
	1	2	3	4	5	6	7	8	9	10
Income tax and VAT	100%	90%	80%	70%	60%	50%	40%	30%	20%	10%
SSC	50%	50%	40%	40%	30%	30%	20%	20%	10%	10%

In terms of compliance rules, RIF taxpayers fill out tax returns every other month, compared to every month in the mainstream tax regime. Moreover, participants can keep their books through an online government tool called "my accounts" (mis cuentas) and use the same information to submit their simplified tax returns. Finally, participants may obtain preferential access to other government programmes such as subsidized credit and training programmes.

Source: Marchese (2021).

► **Box 22: India's 'Hindu Undivided Family' (HUF) regime**

Target group: Households as defined by the Indian tax code.

Eligibility: Based on caste (Hindus, Jain, Sikh and Buddhist families).

Policy description: An HUF is recognized as a separate assessable entity under the Act. Its income may be assessed if following two conditions are satisfied: i) There should be a coparcenership. In this connection, it is worthwhile to mention that once a joint family income is assessed as that of HUF, it continues to be assessed as such in subsequent assessment years till partition is claimed by coparceners. ii) There should be a joint family property which consists of ancestral property, property acquired with the aid of ancestral property and property transferred by its members. Ancestral property may be defined as the property which a man inherits from any of his three immediate male ancestors, i.e. his father, grandfather and great grandfather. Therefore, property inherited from any other relation is not treated as ancestral property. Income from ancestral property held by following families is taxable as income of HUF.

Source: Income Tax Department, Government of India (Accessed 10 Oct. 2023).

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