

# REVISITING THE CONCEPT OF STATE-OWNED ENTERPRISES FROM VIETNAM'S PERSPECTIVE

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## **Abstract**

This paper presents the dynamics of the concept of state-owned enterprises in Vietnam, which manifests the changes in ideological orientation relating to the role of the state sector and of the economic management system. Indeed, the economic reform (*Doi moi* policy) and the integration into the global economy have fostered the participation of the private sector in the economy through the process of state-owned enterprise equitization. The analysis of the concept of state-owned enterprises over time however argues that the change, which has been subject to both internal and external impulses over time, is not fundamental as the key element of socialist ideology, the public ownership of the means of production remains the guiding principle of Vietnam's economic development. In other words, the Vietnamese Government continues to its control over the national economy through the operation of state-owned enterprises.

**Keywords:** *state-owned enterprises, Vietnam, state ownership, socialism, reform.*

## **1. Introduction**

State-owned enterprises (SOEs) have been long existed in many countries around the world, and academic literature has examined their role in industrial development policies across countries and over time. In the case of Vietnam, SOEs acquire a special position due to the fundamental socialist principle of the public ownership of the means of production. This article aims to analyze the concept of state-owned enterprises from Vietnam's perspective as provided by legislation over the time. The discussion needs to be put in a wider political and economic context of Vietnam in its different stages of development. The article focuses on the situation of Vietnam after the country's reunification in 1975, thus the legislation to be analyzed are those enacted after this milestone.

The structure of the article comprises three parts with an introduction. The first section provides an overview of the state-owned sector in Vietnam in order to explore its size and contribution to the socio-economic development of the country. The next section analyzes the evolution of the concept of SOEs in different periods of development. Despite frequent revisions of the laws and the definition of SOE due to both internal and external impulses, there has been no fundamental change in the Party-State leaders' view on the nature of SOEs. The socialist ideology remains the formal guiding principle of Vietnam's economic development. Concluding remarks will be provided in the final section to recap the main points of the article.

## **2. Overview of the state-owned sector in Vietnam**

After the independence of the North in 1954, the Democratic Republic of Vietnam (DRV) adopted and gradually developed the Soviet-style political-economic system, which is referred to by some scholars as the “facsimile of the Soviet command economy, with few concessions to local conditions” (Hoang, 1987; Tran, 1987). By the announcement of a three-year economic plan in 1958, Vietnam pursued a model of state-driven development which relied on state-owned enterprises for its industrialization. By mid-1960s, the economy of North Vietnam was primarily based on public ownership of the means of production and a command management system where the government made economic decisions. After the unification in 1975, the Communist Party of Vietnam (CPV) imposed the Soviet-type organization of the state and the economy on the South, adopting a centrally planned economy with agricultural collectivization, strong capital accumulation, and SOE-led industrialization (OECD, 2022). During this period, SOEs in Vietnam were formed in three ways (Ngo, 2001). First, SOEs were formed by the nationalization of private capitalist enterprises or the takeover of businesses left by the old regime. The second type of SOEs were those which were established by direct investment of the central government from the state budget or foreign construction aid. SOEs of this type were entitled to use technologies and equipment imported from other socialist countries, especially the Soviet bloc and China, and gradually dominated most of the important industrial and service sectors. The remaining SOEs were formed by local governments in accordance with the decentralization policy up to the 1980s. SOEs experienced a massive growth due primarily to the increase in the number of small-sized enterprises in commercial and service sectors (Hong Hanh Le, 2004; Ngo, 2001). As of 1990, there were 12,084 SOEs dominating most industries such as energy industry, including electricity, coal, oil and gas, mining, metallurgy, the chemical industry, and pharmaceuticals (Ngo, 2001, pp. 81–82). In major consumer goods manufacturing such as fabric, paper, bicycles and soap, SOEs accounted for the largest proportion with 70%, 85%, 70% and 60% respectively (Ngo, 2001, p. 82). Construction, transportation, import-export trade, and wholesale trade were also dominated by SOEs.

Despite economic achievements and integration, Vietnamese leaders recognized the need to reform the country's SOE sector to obtain greater efficiency and competitiveness. The pursuit of an economic model based chiefly on the principles of central planning and self-reliance quickly proved untenable. Faced with increasing scarcity, poverty and hyperinflation, the country's ruling party initiated the *Doi moi* (the economic renovation) in 1986 to introduce the market mechanism as the organizing principle of the economy. The gradual transformation of the centrally planned economy to a more market-oriented one involved SOE equitization, the preferred Vietnamese term for privatization. The reform aimed to reduce the number of SOEs, increase the efficiency of state capital invested in SOEs, and improve their business operations (Bui, 2006). Beginning modestly in the early 1990s, the equitization program did not take off in earnest until 1998. The number of SOEs declined from about 12,000 in 1989 to about 6,000 by the end of 1995 (Riedel & Turley, 1999), resulting from the insolvency and merger of small SOEs under the control of local governments (Ishizuka, 2013). There was a substantial reduction in the number of SOEs to 3,324 during 2009-2010 (H. C. Le, Cabalu, & Salim, 2014, pp. 172-184). Re-arrangement of existing SOEs into larger groups is another pillar of the reform, aimed at enhancing the scale of operation and increasing the influence of the Central Government (Beeson & Pham, 2012). Decision No.90 and Decision No. 91 of the Prime Minister in 1994 paved the way for the establishment of state economic groups (SEGs) in 2006 to prepare for the global competition that the state-owned sector would meet as part of the WTO accession, and to prevent the erosion of the socialist orientation of the market economy in which SOEs were to play a leading role. By 2015, around 4,500 SOEs had been equitized and 600 remained wholly state-owned, but only 8% of the state ownership had been transferred to the private sector (Vietnam Economic Times, 2016).

In spite of the reduction in non-profitable SOEs, OECD and others have been critical of the slow pace of Vietnam's SOE equitization process. For example, the Prime Minister proposed privatizing 289 SOEs in 2015, however only 29 of the targeted SOEs were privatized in the first quarter of the year (B. M. Ho, 2015). Since 2016, Vietnam entered a new phase of SOE reform to accelerate equitization of the remaining SOEs that are not of strategic interests, and to sell more shares and list equitized SOEs on the stock exchange (Government of Vietnam, 2017a). The aim is to equitize 137 SOEs and divest in 406 joint stock companies and limited liability companies (Government of Vietnam, 2017a, 2017b). In term of ownership, the State was going to wholly own 103 enterprises, to hold more than 50% but less than 65% of charter capital in 27 enterprises, and own less than 50% in 106 enterprises (Government of Vietnam, 2016). Despite a number of changes in policy and regulations, the Government missed all the deadlines for the accelerated SOE reform. The target was to divest 135 SOEs in 2017 and 181 SOEs in 2018, however the respective results were 13 and 52 (VOV, 2019). As of 2019, the number of SOEs and its

shares in all enterprises accounted for 0.31% of the total number of the country's enterprises (OECD, 2022).

SOEs have also experienced a downward trend in several indicators over the past decade. In the period of 2010 and 2019, SOEs' share in turnover in all enterprises reduced from 27.2% to 13.6%; pre-tax profit from 32.3% to 23.2%, consequently resulting in a decrease in their contribution to the state budget from 45.4% to 26.9% (General Statistics Office, 2022). Regardless of these facts, the state-owned sector is still a significant contributor to the national economy compared to domestic private enterprise and foreign direct investment enterprises. SOEs constitute 22.8% of the country's capital, accounting for around 30% of the GDP (General Statistics Office, 2022; OECD, 2020). SOEs remains a significant contributor on the economy through their preferential position regarding the access to credit, land use, and markets (Pincus, 2016, p. 395; Truong & Rowley, 2014, p. 289).

### **3. The evolution of the definition of SOE in Vietnam**

#### ***3.1. The primary criteria: public ownership and SOEs' political functions***

During the centrally planned economy between 1960 and 1986, state economic units operated in form of state-run enterprises (*xi nghiep quoc doanh*) in manufacturing industries, state-run farms in agricultural sector (*nong truong quoc doanh*), and companies (*cong ty*) in trading and service sectors. The term "state-owned enterprise" (*doanh nghiep nha nuoc*) did not exist in official documents during this period, instead there was a legal definition of state-run industrial enterprise (*xi nghiep cong nghiep quoc doanh*) or state-run trading enterprise (*xi nghiep thuong mai quoc doanh*). According to the Charter of State-run Industrial Enterprises promulgated by the Decree No.93-CP of the Council of Government of 1977 (Charter 1977), the term "state-run industrial enterprise" (SIE) was defined as follows:

"State-run industrial enterprises are the material production and business units of the unified socialist economy, which directly produce material wealth for society and create a source of socialist accumulation. Enterprises operate pursuant to political and economic tasks assigned by the Party and the State, ... perform production and business activities according to the State's plans which are decided by the central government based on the main expenditures in consideration of the general balance of the entire national economy, and are formulated on a bottom-up basis.... have legal person status, and operate on the principle of financial autonomy."<sup>1</sup>

The above definition manifested the traditional socialist ideology which was characterized by two key principles: public ownership of the means of production, and central planning (Beresford & Fforde, 1997; Smith, 1957). The socialist economic order could first be seen in the Chapter II of the 1959

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<sup>1</sup> Articles 1 and 2, Charter of State-run Industrial Enterprises of 1977.

Constitution of the Democratic Republic of Vietnam, with the following noteworthy provisions: (i) the State shall lead all economic activities under a unified plan (Article 10); (ii) the state-operated economy shall play the leading role in the national economy (Article 12); and ownership by the entire people means ownership by the State (Article 11). Following the reunification in 1975, the Constitution of the Socialist Republic of Vietnam of 1980 stipulated a strong commitment towards the State's control over the national economy through a rigid command system (Article 33), and emphasized the construction of a national economy consisting mainly of two sectors: the state-operated economy (*kinh te quoc doanh*) under the entire people's ownership, and collective economy under the collective ownership of laboring people (Article 18). In other words, the first criterion to define a SIE was that it was subject to public ownership, meaning state ownership. The management and use of assets allocated by the State to enterprises were strictly pursuant to the reporting system to the competent authorities.<sup>2</sup> Also, it was the duty of the enterprise and its employees to respect and protect the enterprise assets which were in fact the State assets.<sup>3</sup> Second, the definition emphasized the political functions of enterprises in the state sector. SIEs' operation was subject to the central-planning system. Production demand was determined by the subjective consideration of the planning agencies, and SIEs were obliged to achieve the planned targets assigned by the State. On the one hand, state enterprises were granted a special status in the economy due to their political obligations to fulfill the State's economic plans, given the non-existence of a proper market mechanism at that time. On the other hand, they were granted only a low level of business autonomy, although the legal instruments asserted to encourage their proactive role in terms of production and business plans.<sup>4</sup>

From the mid-1980s, Vietnam suffered steep reduction in Soviet bloc assistance, causing shortage of resources allocated to SIEs through the central-planning apparatus. To survive the economic hardship, Vietnam's leaders announced the economic and political reform in 1986 which focused on the management of state enterprises. The Charter 1977 was replaced by the Charter of State-run Industrial Enterprises of 1988 promulgated by the Decree No. 50-HDBT of the Council of Ministers (Charter 1988). Accordingly, the definition of SIE was revised:

“State-run industrial enterprises (including independent enterprises and union of enterprises) are the economic units, the basic link of the socialist national economy; are the units of planned production of goods to meet the growing demand of society; have legal person status and are subject to independent cost-accounting.”<sup>5</sup>

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<sup>2</sup> Articles 6 and 7, Charter of State-run Industrial Enterprises of 1977.

<sup>3</sup> Article 10, Charter of State-run Industrial Enterprises of 1977.

<sup>4</sup> Articles 4, 20, and 39, Charter of State-run Industrial Enterprises of 1977.

<sup>5</sup> Article 1, Charter of State-run Industrial Enterprises of 1988.

Although SIEs maintained the core elements of state ownership and the political function in which they play the leading role in the nation's development, there were certain legal improvements to place them on a commercial footing for improving their efficiency. The new addition of the Charter 1988 was that while "the entire people" retained ownership over SIEs, enterprise assets were "trusted by the State to the collective of workers headed by its Director for the management and utilization".<sup>6</sup> The Charter of 1988 also made an attempt to categorize enterprise assets by sources, including assets belonging to capital from state budget, and those formed by other sources.<sup>7</sup> The classification however did little help to clarify the ownership of assets in SIEs, because there was no clear differentiation between state capital and an enterprise capital, resulting in legal ambiguities about the ownership of the capital or profits that were raised in the course of doing business (Lee, 2015, p. 201). On the positive side, the State opted to trim its control over SIEs by allowing them a greater degree of operational autonomy.<sup>8</sup> The old idea of central planning was loosened, with SIEs no longer being subject to plans set by the central authorities. In terms of financial autonomy, SIEs could sell, transfer, or lease assets that were not in use or not being used at full capacity, though the sale of fixed assets was prohibited because they belonged to state capital.<sup>9</sup> SIEs were also entitled to participate in direct or indirect exporting activities, which were previously performed exclusively by exporting enterprises under the Ministry of Foreign Trade.<sup>10</sup> Finally, SIEs were granted the right to enter into business alliances and joint ventures. Joint-venture enterprises (*xi nghiep lien doanh*) were introduced as a new form of cooperation between SIEs and enterprises of other economic sectors. The joint-venture model was approached similarly to joint-stock company, a common form of business entity in a market economy. However there were two different sets of regulations applied to this type of business. According to the Decree No. 28-HDBT of the Council of Ministers of 1989, a joint-venture enterprise with more than 50% of shares owned by the State was subject to the regulation of a SIE, otherwise it was regulated by the Decree No.27-HDBT of 1988 promulgating policies for individual economic sector (*kinh te ca the*) and private economic sector (*kinh te tu nhan*). Joint-venture enterprises saw a little development during this period due to the inherent shortcomings of the planned economy

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<sup>6</sup> Article 5, Charter of State-run Industrial Enterprises of 1977.

<sup>7</sup> According to Article 4 of the Charter of State-run Industrial Enterprises of 1988.

<sup>8</sup> Greater managerial autonomy of state enterprises was supported by the Decision No. 217/HDBT of the Council of Ministers of 1987, which provided for reformatory policies for socialist business planning and cost-accounting of state enterprises with the most noteworthy rights such as the right to make investment decision, the right to dispose of assets, the right to hire workers and distribute wages and bonuses.

<sup>9</sup> Article 5, Charter of State-run Industrial Enterprises of 1988.

<sup>10</sup> Article 55, Charter of State-run Industrial Enterprises of 1988.

and the dominance of state enterprises in the economy (Hong Hanh Le, 2004, pp. 75–76).

### ***3.2. New approach in the context of the shift to a multi-sectoral economy***

In the early 1990s, the Vietnamese economy was recovering from hardship and retained very little of the formal system of centralized planning (Fforde, 2021, p. 571). The Party-State pushed for the transition to a market-oriented economy which implied the changing role of the State in the economy. Since the Extraordinary Plenary Session of the 7<sup>th</sup> National Congress of the CPV in 1994, the term “state-operated economy” was replaced by the term “state-owned enterprise sector” so as to manifest the view that the State held the ownership but did not directly instruct the day-to-day management of enterprises (Ha Minh, 2013). The Party also initiated the reform for a “multi-sectoral economy” which was reflected in the Constitution of 1992.<sup>11</sup> Although the dominant role of the state economic sector in the economy was constitutionally preserved,<sup>12</sup> the growth of household and private businesses<sup>13</sup> and the existence of foreign investment were gradually tolerated.<sup>14</sup> As a result, state enterprises faced the challenge to improve their performance efficiency to meet the competition with businesses in the non-state sector. The new political and economic landscape called for a more robust legal framework for the operation of state enterprises so as to fulfill their role in the national economy. The term “state-owned enterprise” was defined for the first time in the Law on State-Owned Enterprises of 1995 (Law on SOEs 1995):

“State-owned enterprise means an economic organization which is capitalized, established, organized and managed by the State, and carries out commercial activities or provides public utility aimed at achieving the socio-economic objectives assigned by the State. A state-owned enterprise shall have legal person status, have its own civil rights and obligations, and take responsibility for all of its activities in business operation within the limit of the capital placed under its management...”<sup>15</sup>

Similar to the previous legal instruments, the Law on SOEs 1995 emphasized the state ownership criterion, and at the same time clarified the establishment, organization, and management by the State. There were however different opinions about the responsibility of the State to provide

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<sup>11</sup> Article 15, Constitution 1992: “The State develops a multi-sectoral commodity economy functioning in accordance with market mechanism under the management of the State and following a socialist orientation. The multi-sectoral economic structure with various forms production and business organization is based on a system of ownership by the entire people, collectives, and private individuals, of which ownership by the entire people and ownership by collectives constitute the foundation”.

<sup>12</sup> Article 19, Constitution 1992.

<sup>13</sup> Article 21, Constitution 1992.

<sup>14</sup> Article 25, Constitution 1992.

<sup>15</sup> Article 1, Law on SOEs 1995.

capital to SOEs. Some criticized that such capital provision was in fact a form of state subsidy which caused an unlevel playing field between SOEs and non-state enterprises, whereas other argued that capitalization aimed to establish ownership of the State over a SOE, along with the rights and obligations of the owner, i.e. the State, in running the enterprise (Bui, 2000, p. 32). The Law also said nothing about the level of statutory capital that the State should provide so as to establish its ownership over an enterprise. To address this problem, the Government issued the Decree No. 59-CP of 1996, specifying that: “Part or the whole of the initial charter capital of a newly established state-owned enterprise shall be provided by a competent state agency, and must not be lower than the total statutory capital of the business lines conducted by the enterprise”.<sup>16</sup>

The Law on SOEs 1995 affirmed SOEs as independent entities in the economy with legal person status, civil rights and obligations, and responsibility for all of business activities. As such, the Law clarified responsibilities and accountability, and established SOEs as limited liability entities. In other words, there should be a separation of ownership and management, and a separation of enterprise property. Regarding the first aspect, the Law on SOEs 1995 specified the rights and role of state management agencies and the collective of workers in day-to-day decision-making. SOEs had the right to “transfer, lease, rent and mortgage properties under their management, except important equipment and factories that are prescribed by the State...and land and natural resources”<sup>17</sup>. While SOEs’ autonomy in day-to-day management decisions, in mobilizing capital, and in allocating profits was guaranteed within state guidelines; the State retained powers to exercise ownership rights in SOEs such as making decisions on business development plan, capital structure, allocation of profits, management structures, appointment of senior management positions.<sup>18</sup> The Law on SOEs 1995 however did not make clear the legal nature of “delivery of state capital” (*giao von*). The act of delivery of capital could be interpreted in different ways: 1. the State, in the same way shareholders of joint-stock companies and member of limited liabilities, transferred the title of capital and assets to SOEs; or 2. the State delegated powers to a competent apparatus to manage the delivered capital in a SOE; or 3. the State hired a competent apparatus to manage the delivered capital in an SOE.<sup>19</sup> Consequently, it was difficult to clarify the rights and responsibilities of the State as the owner of SOEs. Moreover, the Law provided that the transfer, lease, rent and mortgage of important equipment and factories prescribed by the State were subject to the

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<sup>16</sup> Article 3, Decree No. 59-CP.

<sup>17</sup> Article 6(2), Law on SOEs 1995.

<sup>18</sup> Article 27, Law on SOEs 1995.

<sup>19</sup> For more detail, see Bui, V. D. (2000). Ban ve khai niem doanh nghiep nha nuoc theo Luat Doanh nghiep nha nuoc [Definition of State-owned Enterprise under the Law on State-owned Enterprises]. *Tap Chi Quan Ly Nha Nuoc*, 10, 32–35.

approval of the competent state authorities, meaning that SOEs did not enjoy property rights to the fullest, instead they only had the right to use.

Regarding the second aspect, the definition was an effort to end the debatable confusion about the limited or unlimited liability of the State over SOEs. However, the practice showed little improvement as the State continued to charge off and cancel debts to rescue SOEs suffering losses (Bui, 2000, p. 35). Another way for SOEs to survive was for state-owned commercial banks to lend a SOE in financial difficulty even more than charter capital as approved by the competent agency which decided the establishment of that SOE. Most of loans were without mortgage and soon became bad debts. A report found that lending for the most un-profitable SOEs in 1998 and 1999 increased by 138% and 202% respectively, in comparison to 1997 (Bui, 2000, p. 35).

Another noteworthy change is that SOEs were classified into two types: commercially-oriented SOEs and public utility SOEs. A public utility SOE was defined as “an SOE that manufactures and provides public utility pursuant to state policies, or is directly involved in the discharge of defense or security tasks”.<sup>20</sup> Some commentators claimed that the criterion of the nature of activities carried out by SOEs contained legal-economic significance, because it implied the equal treatment between commercially-oriented SOEs and non-state enterprises, as well as the necessarily differentiated approach to public utility SOEs (Hong Hanh Le, 2004, pp. 79–80). In principle, commercially-oriented SOEs are profit-driven entities which must be subject to market rules like enterprises of other economic sectors. SOEs suffering loss and poor performance should be withdrawn from the market. The classification of SOEs paved the way for the State to divest from commercially-oriented SOEs, and on the other hand applied necessary preferences to public utility SOEs which operated pursuant to the State’s policies. The classification however resulted in several confusions. First, the conflict between key legislation over the concept of enterprise (*doanh nghiep*). The Law on Enterprises 1990 provided for a general definition of enterprise as “an economic organization having its own name, having assets and a permanent transaction office, and having business registration in accordance with law for the purpose of conducting business operations”.<sup>21</sup> In contrast, the Law on SOEs 1995, by providing for public utility SOEs, recognized economic organizations which operated without the primary purpose of conducting business activities as enterprises. Some observers also questioned the logic of including public utility enterprises under the regulation of the Law on SOEs. They argued that the State invested in public utility enterprises for the provision of essential goods and services of the public interest rather than for profits, thus it was infeasible to apply legal person status to such enterprises so that they had civil rights and obligations and took responsibility for all of their performance results (N. P. Nguyen,

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<sup>20</sup> Article 3(4), Law on State-owned Enterprises 1995. More detailed definitions were subsequently provided by Decree 56-CP of 1996 on Public Utility State Enterprises.

<sup>21</sup> Article 3(1), Law on Enterprises 1990.

1997). Moreover, the Law on SOEs 1995 did not specify commercial activities of the public utility SOEs, i.e. their investment in other profit-oriented enterprises. There were no clear criteria to differentiate SOEs that were carrying out purely public utility activities and those carrying out both public utility and commercial activities, resulting in the risk of abuses which might negatively impact the competitiveness between businesses of different economic sectors. In practice, the classification of SOEs as public utility and commercial-oriented enterprises was delayed due to the absence of criteria and clear allocation of responsibilities for the process (Arkadie & Mallon, 2003, p. 131).

### ***3.3. Broadening the concept of SOE to speed up the equitization process***

The economic reform guided Vietnam through the period of difficulties associated with the Asian financial crisis and the dramatic reduction in domestic investment to achieve resilience and rapid growth in the early 2000s (Fforde, 2005). The liberalization process also led to the growth of private companies<sup>22</sup> and the emergence of a middle class in Vietnam. These marked fundamental changes in the Party-State leaders' understanding of the role of the state economic sector and other sectors of the economy. The Constitution 1992 (amended in 2001) furthered the ideological compromises towards a market economy by replacing the vague term "multi-sectoral economy" with the notion of "socialist-oriented market economy"<sup>23</sup>. The revised Constitution also recognized domestic capitalist sector and its freedom to compete equally before the law<sup>24</sup> and to conduct business<sup>25</sup>. On the other hand, the Party insisted that the state economic sector played a decisive role and was "the main force in international economic integration"<sup>26</sup> insofar as to hold firm to the socialist orientation. Facing increasing pressure to integrate into the global economy, SOEs were expected to become more market- and profit-oriented, to hold the key positions in the Vietnam economy, and to be an important material instrument for the State to orient and regulate the macroeconomy.<sup>27</sup> Therefore, the most significant policy element towards SOEs in early 2000s, which was marked strongly at the Third Plenum of the 9<sup>th</sup> Party Central Committee, was to accelerate equitization of SOEs for a better fulfillment of their missions. To

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<sup>22</sup> It was recorded that around half a million private companies registered since the enforcement of the Law on Enterprises 1999, which recognized the right to conduct business as part of citizens' liberties. See Pham, D. N. (2016). From Marx to Market: The Debates on the Economic System in Vietnam's Revised Constitution. *Asian Journal of Comparative Law*, 11(2), 263–285. <https://doi.org/10.1017/asjcl.2016.16>

<sup>23</sup> Article 15, Constitution 1992 (amended in 2001).

<sup>24</sup> Article 16, Constitution 1992 (amended in 2001).

<sup>25</sup> Article 57, Constitution 1992 (amended in 2001).

<sup>26</sup> Communist Party of Vietnam, Resolution of the Third Plenum of the Party Central Committee under the 9<sup>th</sup> National Party Congress on continuing restructuring, renovation, and development of SOEs, 2001.

<sup>27</sup> *Id.*

facilitate the SOE sector reform, the new law on SOEs was enacted in 2003 (Law on SOEs 2003) with the revised definition of SOEs as follows:

“State-owned enterprise means an economic organization in which the State owns the entire charter capital or holds the controlling shareholding or controlling capital contribution, and which is organized in the form of a state company, joint-stock company or limited liability company.”<sup>28</sup>

Unlike the previous legislation, defining SOEs under the Law of 2003 was not merely based on the criterion of ownership, i.e. enterprises wholly-owned by the State, but it was the controlling shareholding or controlling capital contribution of the State in an enterprise that characterize it as an SOE. The Law stated that the controlling shareholding or controlling capital contribution of the State over an enterprise was determined by the State holding more than 50% of the charter capital.<sup>29</sup> As such, the State held right to decide the operational charter of the enterprise, to appoint, suspend or dismiss key managerial positions in the enterprise, and to organize management and make important management decisions of the enterprise.<sup>30</sup> The revised definition thus broadened the scope of enterprises which would be categorized as SOEs.

The Law on SOEs 2003 repealed the classification into commercial-oriented and public utility SOEs as provided by the former legislation. Instead, the new Law inserted several provisions allowing state companies to participate in public utility operations with specific rights and obligations. For example, they might receive additional investment corresponding to the public utility duties assigned by the State,<sup>31</sup> and at the same time should be accountable to the State for the outcomes of their public utility operations, and held liability to consumers and the law for the public utility products and services that they produced or supplied.<sup>32</sup>

The Law 2003 addressed various forms of SOEs, including:

- (i) State companies (*cong ty nha nuoc*)<sup>33</sup> of which the State held 100% of charter capital;
- (ii) Shareholding companies to be divided into two types: state shareholding companies (*cong ty co phan nha nuoc*) of which all shareholders were state companies or organization authorized by the State to contribute capital, and enterprises with the State

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<sup>28</sup> Article 1, Law on SOEs 2003.

<sup>29</sup> Article 3(5), Law on State-owned Enterprises 2003.

<sup>30</sup> Article 3(8), Law on SOEs 2003.

<sup>31</sup> Article 19(3), Law on SOEs 2003.

<sup>32</sup> Article 19(2), Law on SOEs 2003.

<sup>33</sup> State company means an enterprise in which the State owns the entire charter capital and which is established, and whose management in organized and operations registered pursuant to this Law. State company shall be organized in the form of independent State company or state corporations. Article 3(1), Law on State-owned Enterprises 2003.

- holding controlling shares or controlling capital contribution of which the State held over 50% charter capital;
- (iii) State limited liability companies of which the State owning the entire charter capital, or with two or more members were state companies.

On the surface, this manifested a change in ideology of the Party-State to recognize the equal existence of multi-owner in a SOE and the possibility to convert ownership of State companies in the form of equitization, sale of the whole of a State company, sale a part of a State company, or assignment of a State company to the labor collective for conversion into a joint-stock company.<sup>34</sup> The approach of the Law on SOEs 2003 was expected to pave the way for SOE reform by ensuring the State's control over enterprises in a renovative and more efficient method. It turned out that the conversion of ownership of State companies in practice, especially by means of equitization, was not well supported by the legislation. Although, the Law provided for types of State companies whose ownership might be subjected to conversion,<sup>35</sup> such typologies were set by state decision rather than by the market. The reality, as argued by some commentators, was that ministries and localities were afraid of losing their control over SOEs (Doan, 2002), with their administrative discretion thus slowing down the pace of reform. Another shortcoming was that the Law on SOEs 2003 provided for a dual-regulatory regime applied to different types of SOEs. The Law was named "Law on State-owned enterprises" with a broad definition of SOE as prescribed in Article 1; however, the governing scope was limited to state companies as the remaining types, i.e. shareholding companies and limited liability companies, were registered and operated pursuant to the Law on Enterprises 1999. There were conflicts between these two legislations in regulating SOEs, and in some cases the former neutralized the effect of the latter. For instance, Article 3(5) and (8) of the Law on SOEs 2003 provided that the State holding more than 50% of the charter capital should have controlling rights over that enterprise, including the right to make important management decisions. On the other hand, the Law on Enterprises 1999 required the consent of shareholders or members representing more than 65% of charter capital to approve the important management decisions of a shareholding company or limited liability company. In case of conflict between the Law on SOEs 2003 and the Law on Enterprises 1999 regarding the representative of State's capital contribution, the former should prevail.<sup>36</sup> This provision might result in the improper intervention by the representative of the State's capital contribution during the operation of shareholding companies. SOE equitization became less attractive to the private

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<sup>34</sup> Article 80, Law on State-owned Enterprises 2003.

<sup>35</sup> Article 81, Law on SOEs 2003.

<sup>36</sup> Article 4(2), Law on SOEs 2003.

investors, because little would change in the managerial regime if the State remained the majority shareholder in the post-equitized enterprises.

In 2004, Vietnam faced pressure to hasten the reform of the SOE sector as the WTO negotiation accelerated. By the end of that year, the Vietnamese Government promulgated the Decree No. 187/2004/ND-CP on transforming SOEs into joint-stock companies, but with new stipulations. All SOEs, including both subsidiaries of state-own corporations and the corporations themselves, were to be subject to equitization in case they were not required to be kept entirely under state ownership. In an effort to complete the accession to the WTO, the National Assembly of Vietnam passed the Unified Law on Enterprises in November 2005 (Law on Enterprises 2005), which stipulated that from 1 July 2006 all SOEs would have to be transformed into joint-stock companies or limited liability companies. This would serve as the legal basis for an equal business field for all enterprises, because enterprises regardless of their ownership types should be regulated by a single law, and should be exposed to the market mechanism. Under the Law on Enterprises 2005, SOE referred to an enterprise of which more than 50% of charter capital was owned by the State. The provision was consistent with the threshold prescribed by the Law on SOEs 2003. SOEs established under the 2003 Law on SOEs should be transformed into limited liability company or joint-stock companies in not more than four years from the date of the Law on Enterprises 2005 comes into effect. Therefore, the Law on Enterprises 2005 should be of full force and effect for enterprises regardless of their ownership type from 1 July 2010.<sup>37</sup> For further promotion of SOE equitization, the Government issued the Decree No. 59/2011/ND-CP dated 18 July 2011 on transferring SOEs with 100% state capital into joint-stock companies. The objective of the Decree was to transfer SOEs in which the State did not need to keep 100% of the capital into multi-owner businesses. The Government aimed to mobilize capital from domestic as well as foreign investors to improve financial capacity, technology innovation, and management innovation so that the efficiency and competitiveness of the individual enterprises and the economy would improve.<sup>38</sup> With the assistance of the legal instruments and more determined policy promotion by the Government, the years 2003-2011 became the major period of SOE equitization in Vietnam.<sup>39</sup>

#### ***3.4. The back and forth of legislative thoughts to keep socialist principles alive***

Since the accession to the WTO, Vietnam has become increasingly integrated into the global economy, but has been facing the challenge of

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<sup>37</sup> Article 166, Law on Enterprises 2005.

<sup>38</sup> Article 1(1), Decree No. 59/2011/ND-CP.

<sup>39</sup>The promoting phase between the mid-1998 and 2011 saw a huge number of SOE privatized, accounting for almost 60% of all privatized SOEs over the 25 years of the privatization program. See Le, H. H. (2017). Vietnam's New Wave of SOE Equitization: Drivers and Implications. ISEAS Perspective, 57, 1-8.

keeping up with other advanced economies in the region. There have been growing domestic pressures for a comprehensive institutional reform, especially on disciplining SOEs and promoting the private sector as the driving force of the economy (D. N. Pham, 2016, p. 272). In this context, the Party became aware of the need to revise the economic development policies, and later adopted the Socio-Economic Development Strategy for the period of 2011-2020 at the 11<sup>th</sup> Party Congress in January 2011, which identified three policy priorities, including the revision of the existing Constitution. The new edition of the Constitution passed in 2013 (Constitution 2013) recognizes the decisive role of the market in the national economy, emphasizing the importance of the private sector, and fair treatment among all economic sectors.<sup>40</sup> The Constitution 2013 however contains a major contradiction as it commits to market rules but protects the dominance of the state economic sector.<sup>41</sup>

The second challenge is to redefine Vietnam's current economic growth model which has heavily relied on labor-intensive industries and exploiting natural resources rather than a competitive and innovative growth model. In this respect, the CPV advocates for a deeper and more comprehensive integration into the global economy by signing and acceding to regional free trade agreements (FTAs). FTAs are expected to help Vietnam shift away from exporting low- and primary goods to more complex high-tech goods such as electronic devices and vehicles (Vettoretti, n.d.). Moreover, the 11th Party Congress affirmed Vietnam "to be proactive and active in international integration, to be a friend, a trustworthy partner, and a responsible member of the international community".<sup>42</sup> In an attempt to negotiate significant FTAs, especially Trans-Pacific Partnership (TTP) and EU-Vietnam Free Trade Agreement (EVFTA), Vietnam initiated the revision of its SOE legislation.

The definition of SOEs was once again revised under the Law on Enterprises 2014, which stated that: "State-owned enterprise means an enterprise of which the State holds 100% of charter capital".<sup>43</sup> The Law also provided for a separate chapter to regulate corporate governance of SOEs (Chapter IV), whereas enterprises of which the State holds less than 100% of charter capital were subject to the regulation as enterprises of other ownership types. Unlike the previous legislation, the Law of 2014 only used absolute State ownership to differentiate SOEs with enterprises of other types. The newly enacted definition also significantly narrowed the scope of enterprises to be defined as SOEs, because enterprises in which the State held the controlling shareholding or controlling capital contribution fell outside of the scope of the SOE definition under the Law of 2014. SOEs were only organized in the form of single-

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<sup>40</sup> Article 51(2) and (3), Constitution 2013.

<sup>41</sup> Article 51(1), Constitution 2013.

<sup>42</sup> Communist Party of Vietnam (2011), Instruments of the 11th Party Congress.

<sup>43</sup> Article 4(8) Law on Enterprises 2014.

member limited liability companies where the State was the sole owner. Some claimed that these changes would create a more even playing field between SOEs and non-state enterprises (T. D. H. Nguyen, 2016; T. T. Nguyen, 2017). The State should act as the co-owner or shareholder as other shareholders in an enterprise with less than 100% of charter capital owned by the State, thus the governance of such enterprise would not be different from enterprises in non-state sector. Moreover, they should be subjected to the same regulations as private enterprises, and in principle should be not eligible or qualify for preferential treatment by the State as the owner (OECD, 2022). In other words, the narrow definition of SOEs was justified to improve corporate governance and performance efficiency of the post-equitized SOEs.

However, the real reason for the legislative change was to bring about advantages for Vietnam in the negotiation process of the two major FTAs at that time, i.e. TPP and EVFTA. A statistics in 2014 showed that SOEs held 70% of real estate, 70% of official development assistance, and 60% of lending credits in the economy, but caused 70% of total bad debts in the financial system (Nguyen S., 2014). By the restructuring and sale of the State's share, and applying the newly enacted SOE definition, the number of SOEs would decrease from 700 to less than 300 at the end of 2015 (Nguyen S., 2014), thus the macroeconomic indicators of Vietnam would be healthier. Moreover, by arguing that the number of SOEs decreased significantly and those directly affected by the commitments became smaller, Vietnam would have a greater chance of being recognized as a market economy. Indeed, as the TPP negotiation did not include a concrete definition of SOE, SOE provisions under the Law on Enterprises of 2014 were blurred to avoid the pressure from other TPP negotiators (T. A. N. Le, 2015). Vietnam also attempted to list a considerable number of exceptions to exempt the SOEs' conditions and their activities during the negotiations (Willemyns, 2016, p. 673). Eventually, many of the exceptions were successfully listed in the then Comprehensive and Progressive Agreement of Trans-Pacific Partnerships (CPTPP) (Sakata, 2020).

From 2016, Vietnam entered the new phase of SOE reform. Due to the poor performance of the Vietnamese stock exchange and the time-consuming preparation for the equitization of large SOEs, the SOE equitization moved ahead at a slow pace during 2011-2015. The State carried out the equitization of SOEs and sold part of its shares to the private sector, but overall still maintained a significant capital share in the equitized enterprises, accounting for over 76%, even up to 96% in many cases (V. H. Ho, 2020; G. Nguyen, 2019). The narrow concept of SOE under the Law of 2014 in fact concealed the actual size and influence of the state economic sector in the national economy, and administrative officials had not been forced to withdraw from business activities of the enterprises. Such policies had done little to facilitate the SOE equitization, because the practice of SOE equitization over the years has showed that an equitization plan to reduce the proportion of state capital to less than 50% of charter capital often attract more investors in the private sector (G. Nguyen, 2019). To foster the SOE reform, the Resolution No.12-NQ/TW of the

Central Committee in 2017 on continuing to innovate, restructure and improve the performance of SOEs aimed to accelerate equitization of SOEs that are not of strategic interests and to apply international standards on corporate governance of SOEs. The Resolution introduced a different approach to the definition of SOEs in comparison with the one provided by the Law on Enterprises 2014. “SOE means an enterprise of which the State holds 100% of charter capital, or controlling shares or capital contribution, organizes and operates in form of a joint stock company or limited liability company”.<sup>44</sup> Accordingly, there should be two categories of SOEs: (i) those with 100% of state capital; and (ii) those with less than 100% of state capital but to the extent that State controls the enterprise. Law on Enterprises 2014 needed to be revised in order to institutionalize the Party’s guiding instrument.

In addition, Vietnam has faced external pressure on fulfilling commitments on SOEs under the new FTAs. The SOEs as defined in the Law on Enterprises 2014 was not compatible with the EVFTA and CPTPP trade pacts that Vietnam ratified. EVFTA defines SOEs as an enterprise that:<sup>45</sup>

“...including any subsidiary, in which a Party, directly or indirectly:

- (i) owns more than 50 per cent of the enterprise’s subscribed capital or controls more than 50 percent of the attached to the shares issued by the enterprises;
- (ii) can appoint more than half of the members of the enterprise’s board of directors or an equivalent body; or
- (iii) can exercise control over the strategic decisions of the enterprise.”

Similarly, CPTPP provides for the definition of SOE as follows:<sup>46</sup>

“State-owned enterprise means an enterprise that is principally engage in commercial activities in which a Party:

- (a) directly owns more than 50 percent of the share capital;
- (b) controls, through ownership interests, the exercise of more than 50 percent of the voting rights;
- (c) holds the power to appoint a majority of members of the board of directors or any other equivalent management body.”

The incompatibility between domestic law and international agreements on the definition of SOEs poses the risk that Vietnam may infringe on the rules of subsidies and countervailing measures (T. T. Nguyen, 2017). To live up the motto that Vietnam is “a friend, a trustworthy partner, and a responsible member of the international community,” the revision of SOE definition was necessary.

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<sup>44</sup> Communist Party of Vietnam (2017), Resolution No.12-NQ/TW of the Central Committee.

<sup>45</sup> Chapter 11, EVFTA

<sup>46</sup> Article 17.1, Chapter 17, CPTPP.

The drafting of the revised Law on Enterprise kicked off a fierce debate over the controlling shares or capital contribution held by the State in a SOE. The drafting agency, the Ministry of Planning and Investment (MPI), proposed the threshold of more than 50% of charter capital held by the State. This proposal however stirred up concerns among members of the National Assembly over whether such threshold was enough to ensure the control of the State over SOEs. For example, Representatives from Lang Son province and An Giang province suggested raising the threshold to at least 75% so as to ensure the absolute control of the State over the important management decisions of SOEs (T. Nguyen, 2019). On the other hand, a Representative from Giai Lai agreed with the proposal submitted by the MPI because it was compatible with the one provided by the new FTAs. Eventually, the Law on Enterprises was passed in June 2020 (Law on Enterprises 2020) with the amended definition of SOEs as follows: “a state-owned enterprise means an enterprise of which the State holds more than 50% of charter capital or voting shares”.<sup>47</sup> In addition, Article 88 of the new Law specifies two types of SOEs:

(i) Wholly SOEs include: single-member limited liability companies 100% of charter capital of which is held by the State that are parent companies of state-owned corporations or parent companies in groups of parent company-subsidiary companies; independent single-member limited liability companies 100% of charter capital of which is held by the State;<sup>48</sup>

(ii) Partially SOE include: multiple-member limited liability companies and joint stock companies over 50% of charter capital voting shares of which is held by the State and that are parent companies of state-owned corporations or parent companies in groups of parents – subsidiary companies; independent multiple-member limited liability companies and joint-stock companies that the State holds over 50% of charter capital or voting shares.<sup>49</sup>

Technically, the definition comes back to the one provided by the Law on Enterprises 2005, which is a broad concept of SOEs, resulting in an increase in the size of state economic sector. There were about 1,204 SOEs of which the State held 100% of charter capital in 2018, and by adding SOEs of which the State held more than 50% as provided by the Law on Enterprises 2020, the number might go up to nearly 2,500 SOEs (Nguyen L., 2019). In terms of corporate governance regime, SOEs wholly owned by the State are subject to the provisions under Chapter IV of the new Law, which are generally stricter than those applicable to companies with no state capital. Meanwhile, SOEs having state capital proportion of more than 50% but less than 100% fall within the scope of the regulations applicable to multi-member limited liability or joint-stock companies stipulated in the new Law. The revision is expected to foster the restructuring of SOEs, and to diversify the type of SOEs so as to attract strategic investors (T. H. T. Pham & Tran, 2022), because SOEs are

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<sup>47</sup> Article 4(11), Law on Enterprises 2020.

<sup>48</sup> Article 88(2), Law on Enterprises 2020.

<sup>49</sup> Article 88(3), Law on Enterprises 2020.

entitled, in a limited fashion, to operate as single-member or multiple-member limited liability companies, or joint-stock companies. As such they will have more channels to mobilize capital, funds and other resources from the private sector.

#### **4. Concluding remarks**

The legal definition of SOEs in Vietnam has been subject to frequent revisions (1988, 1995, 2003, 2005, 2014, and 2020) over three decades of economic reform so as to align them with the SOE policies directed by the CPV. The change can be explained by both internal and external impulses. Internally, the inefficient state-led economic model, and the emergence and rapid growth of the private sector led to the transition from a centrally planned economy to a socialist-oriented market economy. The evolution of SOE definition over time indicates that SOEs have gradually become independent economic entities and commercially oriented. SOE policies have also changed in correspondence with external pressures to integrate to the global economy. Evidently, at the stage of the negotiation for WTO accession, Vietnam made a great effort to improve its legal framework on business environment, including the amendment of the SOE definition under the Law on Enterprises of 2005. In a recent development, for better compatibility with the commitments of major free trade agreements such as EVFTA and CPTPP, Vietnam recently provided for the revised legal expression of SOE under the Law on Enterprises of 2020. Thus, it is widely said that SOE reforms in Vietnam have been ushered by the international trade commitments (Hong Hiep Le, 2015; World Bank & Ministry of Planning and Investment of Vietnam, 2016).

The paper however contends that there has been no fundamental change in policy-makers' view on the nature of SOEs. The *Do moi* officially abandoned some aspects of the centrally planned economy (Gillespie, 2018, p. 322), yet the key element of socialism have been reformed and retained: public ownership of the means of production. Vietnam has politically and legally affirmed the leading role of the state economic sector in the national economy, and the State exercises its economic functions through the operation of SOEs. Under the internal and external pressures, the Party-State has been constantly revised the SOE policies in different periods of development, but has not addressed the core issues. Some characterizes the regulation of SOEs in Vietnam as a “fluid context-driven phenomenon” which are selectively and erratically used to achieve the pragmatic policy priorities (Fforde, 2005). This can be demonstrated by the contradict approaches to SOE issues during the WTO and TPP negotiations. In the former case, the SOE concept was broadened under the Law on SOEs 2003 and Law on Enterprises 2005 so as to foster the SOE equitization and to cut down preferential treatment for state-invested enterprises. The legislative thoughts however shifted to narrow the scope of state-owned sector so as to reduce the number of SOEs that would have been affected by the TPP negotiation. Another evidence is the process of equitization of SOEs. Vietnam prefers the term “equitization” to

“privatization”, because it aims to convert SOEs into joint-stock enterprises where the State remains the sole or majority shareholder rather than the full privatization of SOE supported by neo-classical economic theories. Vietnam has set targets to reduce its direct ownerships in SOEs and promote private ownership, nevertheless SOE equitization has not yet taken place as scheduled and has encountered continuous delays (Guild, 2021). Foreign investors have especially faced major hurdles, including the inability to acquire a controlling interest and postponement in the transfer of ownership (Guild, 2021). The frequent changes of the legislation on enterprises provide a low level of legal certainty for the private investors who intend to participate into SOE equitization. The Government has revised the legal expression of SOEs several times, which may broaden or narrow the scope of SOEs and thus impact the process of equitization of SOE. As a commentator described, the track record of equitization in key industries in Vietnam is two steps forward and one step back (Guild, 2021), because the Vietnamese Government is reluctant to reduce its intervention over SOEs. All in all, because socialism remains the formal guiding principle of the economic development in Vietnam, it thus shapes the law (Fforde, 2005, p. 254) as can be seen from the analysis associated with the concept of SOEs.

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