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Streamlining Business Startup through Effective Implementation of the Enterprise Law

Background

IFC-MPDF's Business Issues Bulletin of July 2006 highlighted some of the important ways in which the Enterprise Law's promulgation in December 2005 will change the business registration process in Lao PDR. It also emphasized that the passage of the law is just the first step of the reform process, and that the law's tangible impact will only be observed after the necessary implementing regulations are issued and enforced. One of the Enterprise Law's main achievements is that it requires a change from the current government practice of requiring all firms to obtain operating permission from the relevant line ministries before business registration to a system in which firms register initially with the Ministry of Industry and Commerce (MOIC) and are subsequently monitored by the appropriate sectoral agencies. In order to implement this shift, the Government first needs to establish a "negative list."

What is the "negative list"?

Article 2 of the Enterprise Law defines the "negative list" as a list of highly sensitive business activities (e.g., national security, public order, cultural traditions and the environment) in which entrepreneurs are subject to inspections by the relevant sectoral agencies before they can register a business. In effect, it is a list of conditional business activities that will continue to require prior approval from relevant government sectoral agencies before registering and starting operations. According to the Enterprise Law, all businesses involved in activities excluded from the "negative list" do not require prior approvals and are only required to register with MOIC. This shift from the previous *ex ante* registration system, in which businesses must obtain prior approvals from the government, to an *ex post* monitoring system, in which businesses register first and are then regulated by the line ministries is the Enterprise Law's principal reform. Figure 1 illustrates the new registration process as mandated by the Enterprise Law.

IFC-MPDF is assisting the government with the development of clear and transparent criteria for "sensitive" business sectors (as defined in Article 2 of the Enterprise Law). Only with such standards will it be possible to ensure that the "negative list" is concise and allows no room for discretion by

government officials. IFC-MPDF recommends that these criteria be based on the following considerations:

National security - impact on national defense, the military and protection of borders;

Public order - significant impact on the country's economic and political stability, which makes it important for the government to control market entry in this area. Businesses under this criteria may be subject to minimum capital requirements or a concession agreement;

Cultural traditions - related to the cultural norms and practices in Lao PDR; and

Environment - related to the exploitation of natural resources and/or causing significant environmental impact. In many cases, concession agreements may be involved.

To ensure clear identification of the business activities on the "negative list" and that there will be no room for discretion in determining the relevant registration procedures, IFC-MPDF recommends that the government apply the United Nations Industrial Standard International Classification of All Economic Activities (ISIC Revision 4 December 2005) when preparing the negative list. All business activities on the "negative list" should be identified using this standard classification system.

MOIC has established a taskforce to develop the "negative list." Based on preliminary discussions, it appears that examples of activities on the "negative



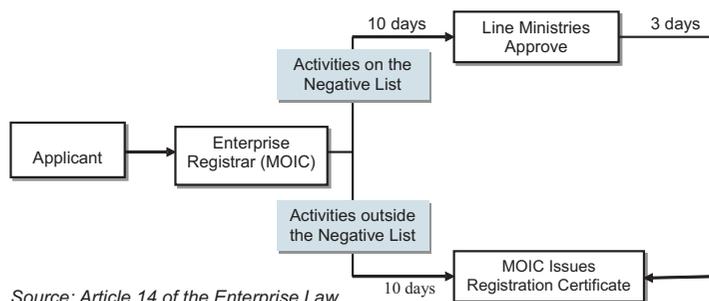
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The "Business Issues Bulletin" provides those interested in business issues with a short summary and analysis of a particular topic affecting the business environment in Lao PDR, and exposure to different opinions held by various stakeholders on the topic.

The statements and opinions presented here are only meant to provide additional reference material and do not reflect official opinion of the Lao National Chamber of Commerce and Industry (LNCCI) or IFC-MPDF.

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Figure 1: Business Registration Process under the New Enterprise Law



Source: Article 14 of the Enterprise Law

list” would include logging and mining (i.e., activities related to the exploitation of natural resources and involving concession agreements); banking and insurance (activities requiring minimum capital); gambling and betting (activities related to public order and stability); and the manufacture of weapons and fighting vehicles (activities related to national security). However, as the MOIC taskforce is still in the early stages of preparing the list and relevant line ministries will need to be consulted during the process, it is difficult to predict which activities will be on the final “negative list.”

Process for preparing the “negative list”

On October 24, 2006, the Prime Minister issued PM Order No. 37/PMO on the Implementation of the Enterprise Law, which assigns MOIC the lead in coordinating the relevant line ministries to implement the Enterprise Law and sets out a timeline for developing the “negative list.” In order to fulfill the Prime Minister’s order and implement the Enterprise Law the MOIC issued Instruction No. 1577 in November 2006, which assigns the Small and Medium Enterprise Promotion and Development Office (SMEPDO) to coordinate the process for developing the “negative list” and other relevant forms for enterprise registration. An inter-Ministerial team composed of mid- to high-level officials is preparing the final draft of the “negative list,” which according to the PM Order, should be approved by the end of the first quarter of 2007.

Impact of an effective “negative list”

Under the current system, starting a business in Lao PDR involves many steps and interactions with multiple public sector entities at different levels of government. A major step in the process is obtaining an establishment license before registering at MOIC. Several line ministries are involved in this process, since all relevant regulatory agencies must approve the establishment of an enterprise. This requirement significantly increases the number of days and government visits involved in registering a business.

Table 1 summarizes the minimum/official number of days and visits it takes to establish a domestically-owned hotel, garment factory and food processor in

Lao PDR. As can be seen in this table, the elimination of the establishment license for all business activities excluded from the “negative list” would significantly reduce the time and visits needed for startup. For example, effective implementation of the negative list would reduce the number of days needed for a hotel to startup by 71 days while garment manufacturers and food processors would require 35 fewer days to start operations.

Next steps to improve business startup procedures

Although the Enterprise Law will significantly streamline business startup procedures, further improvements to business related regulations are still needed to help Lao PDR compete successfully for investment with other countries in the region. Reconciling conflicts between the Enterprise Law and other commercial laws, streamlining licensing procedures and developing a national business registry will be priority areas in the next round of improving business regulations to reform market entry for firms in Lao PDR.

A. Harmonization of laws

Further improvements to the Domestic and Foreign Investment Promotion Laws and their implementing regulations are needed to harmonize them with the Enterprise Law’s policy of facilitating business startup. These improvements should reduce the number of steps for applicants under each law and increase transparency at each step for the benefit of both the entrepreneurs involved and the officials of the relevant ministries and local governments administering the laws and regulations.

The areas that most need improvement are the following:

While the implementing regulations for the new enterprise law are intended to contain a “negative list” which clearly defines business activities that require prior approval from relevant agencies, the two existing Investment Promotion Laws apply a “positive list” which requires investors to seek approval to operate activities in both open and conditional categories. Presumably the newer “negative list” approach in the Enterprise Law is

Table 1: Startup Procedures for Hotel, Garment and Food Processors

Steps	Ministries*	Number of Days			Number of Visits to Government Agencies			
		Hotel	Garment	Food	Hotel	Garment	Food	
1	Establishment license	Line ministries	71	35	35	8	4	4
2	Construction permit	Ministry of Communication, Transport, Post and Construction	45	45	45	2	2	2
3	Enterprise registration certificate	Ministry of Industry and Commerce	2	2	2	2	2	2
4	Tax certificate	Ministry of Finance	10	10	10	3	3	3
5	FDA certificate	Food and Drug Administration			44			2
6	Operating license	Line ministries	66	25	25	3	1	1
7	Company seal	Ministry of Public Security	12	12	12	2	2	2
8	Company sign	Ministry of Information and Culture	10	10	10	1	1	1
9	Social security registration	Social Security Agency	3	3	3	1	1	1
Total			219	142	186	22	16	18

Note: Most licenses and permits are currently issued by sectoral agencies at provincial level.
Source: IFC-MPDF Study on Business Registration Licensing in Lao PDR, February 2006

intended to replace the “positive list” approach in the Domestic and Foreign Investment Promotion Laws. If so, the two investment laws or their implementing regulations will need to be revised.

For other laws and regulations that affect business startup and operation, such as the Manufacturing Law and the Tax Law, it is necessary to increase transparency through development of provisions that set standards and then provide for an appropriate form of verification of compliance with such standards. The provision for such form of verification should clearly specify whether the verification is required before or after a business starts up its operations.

B. Streamlining licensing procedures

To simplify business startup procedures further in Lao PDR, the government should undertake the following four basic steps: i) reduce the number of business licenses and other regulatory documents that are required for startup; ii) simplify the remaining application documents and procedures; iii) better integrate elements of the registration and licensing procedure into a more coherent system; and iv) remove the requirement that operating licenses be renewed annually. These measures can be achieved in large part by eliminating unnecessary duplication (such as in the information and attachments that are required on official forms), reducing paperwork and allowing the market to be the main arbiter of business success or failure in the vast majority of (non-strategic) business sectors. The implementation of a regulatory review process would assist to reduce the burden of regulation on the private sector by identifying measures for streamlining licensing procedures and eliminating unnecessary requirements.

C. Establishing national business registry

In the near future, a national business registry should be developed to provide policymakers with accurate and up-to-date information so that they

can monitor enterprise creation more efficiently. This information can also be useful to the private sector, as it would include data on registered businesses and facilitate the development of business networks. Over the longer term, a national business registry should also link to data held by other relevant ministries/agencies to facilitate information sharing and for the purpose of enhancing regulatory efficiency. For example, one of the government's long-term objectives should be to have every business use a single common registration and tax identification number.

Conclusion

The transition from ex ante to ex post regulatory practices in Lao PDR constitutes a major improvement to the business environment and represents a significant step towards the implementation of a system based on international good practice. The development of a clear and concise “negative list” is an integral part of this transition. Not only will the list help achieve reforms such as streamlining paperwork and reducing the time needed to register enterprises, but it will also result in better regulation. The reforms resulting from effective implementation of the Enterprise Law will reduce the burden of regulation on businesses and result in more effective and efficient ex-post monitoring for businesses. Harmonizing the legal framework will ensure that regulations are implemented in a consistent manner and with limited discretion on the part of government officials. The end result will be a system that encourages more

businesses to startup while at the same time improving the effectiveness and efficiency of the regulatory process.

Viewpoint from the Government

Under the new Enterprise Law, investors who are interested in areas that are excluded from the “negative list” of closed or conditional sectors may expect their businesses to be registered with the Ministry of Industry and Commerce within ten days of submitting their application. In other words, one can establish a business in unrestricted sectors before having to obtain the necessary operating licenses and permits. By reducing the administrative burden faced by entrepreneurs, this improvement in official registration and startup procedures will encourage more business activity.

Businesses operating in those sectors that are included in the “negative list” will continue to require prior approval from relevant line ministries before commencing operations. For this reason, in order to effectively implement the Enterprise Law, it is important that the “negative list” be short, very specific and comply with the spirit of the law, which is that in general, businesses should be allowed to register first before having to obtain regulatory licenses and other permits. As we develop the negative list, I would like to emphasize that our focus is on achieving better regulation of businesses as opposed to removing regulation. After all, as we all agree, regulation is a very important function of the Government.

Mr. Siasavath Savengsuksa, Vice Minister of Industry and Commerce. Remarks are from the December 2006 Consultation Workshop on the Development of the “Negative List” under the Enterprise Law.

Viewpoint from the Business Community

There is evidence that easier business startup procedures can help generate more business ventures and create a more dynamic private sector. According to the World Bank’s Doing Business 2007 report, forty-three countries made it easier to start a business during 2006. Of these, seven countries reduced or eliminated the minimum capital requirement, and we are very pleased that Lao PDR was among them.

However, while improved business registration is necessary to encourage the formalization of enterprises, it is only one aspect of the overall business environment. In some cases, it may not be sufficient to spur further private sector development, as taxes may still be too high or access to credit may be a cumbersome process. Therefore, we would like

to encourage the Government to continue its efforts towards further improving the business environment in Lao PDR and implementing reforms in other areas besides business startup procedures.

Mr. Khunthavong Dalavong, Secretary General of the Lao National Chamber of Commerce and Industry.

Viewpoints from International Experts

The Government’s efforts to streamline business startup procedures are highly commendable. This should improve the ability of private firms to invest more, be more productive, and create jobs. Agreeing on a short, clear-cut, and tightly defined negative list of sensitive business activities requiring prior approval from sectoral agencies before registration, rather than imposing this requirement on all prospective new businesses, seems to be a step in the right direction.

Mr. Geoffrey Walton, Senior Investment Policy Officer, FIAS, World Bank Group

The Enterprise Law and its implementing regulations are important steps for facilitating business in Lao PDR. The Prime Minister’s Order No. 37/PMO forbids anyone from adding to the steps or extending the duration for approval of business registration beyond what is already provided in the Enterprise Law. This is a very useful provision but its usefulness is limited by the fact that it does not apply to the whole business startup process but only to the part related to enterprise registration.

The other laws and regulations related to startup of businesses besides the Enterprise Law need similar provisions to ensure that businesses are able to startup freely. At the same time, the whole population of investment and sectoral regulations that affect business startup need to be reviewed to determine which steps and requirements are still necessary and which steps and requirements can be combined or eliminated. Some of the steps and requirements that are still necessary can be made less burdensome by being made subject to verification after a business is up and running rather than before it starts up. With clear startup provisions and a regulatory review process, the burden of business regulation can be reduced. That reduction should result in more businesses starting up and being more successful.

Mr. John Davis, International Lawyer.