

*An Overview of the Legal, Regulatory and Institutional Framework of Mongolia's Mining Industry**

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Introduction

Mongolia, a resource-based developing economy, is making bold steps toward becoming a mining hotspot in the region. From the early 2000s, the country has attracted a noticeable share of the world mineral exploration investments thanks to its liberal minerals law, and favorable world commodity market conditions. This paper introduces and examines the regulations of the laws in Mongolia in relation to establishing and operating a mining company.

Mongolian Laws and Regulations Relating to Exploration for Minerals and Mining

Between July 1997 and 25 August 2006 Mongolian minerals policies and practices were governed by the 1997 Minerals Law. On 8 July 2006, the parliament of Mongolia (the State Great Khural) enacted the 2006 Minerals Law, superseding and replacing the 1997 Minerals Law. The 2006 Minerals Law became effective as of 26 August 2006 and it became the main law for the mining sector of Mongolia.

Mongolian Exploration Licenses

The holder of an exploration license has rights to access the license area through public or private property (subject to the need for negotiated approvals by owners, possessors and users of such property), to conduct exploration and construct temporary structures within the license area and, if a mineral resource is defined by exploration activities, to apply for a mining license for any part of the exploration license area. Pursuant to the 2006 Minerals Law, exploration licenses granted on or after 26 August 2006 have an initial term of three years. The holder of such an exploration license may apply for an extension of the license for two successive additional periods of three years each. Thus, the maximum period that an exploration license may be held by one or more holders is nine years from the date of issue.

Each exploration license is subject to cancellation if applicable license fees are not paid on time or if the holder fails to comply with certain other requirements of the 2006 Minerals Law or other relevant laws. Only Mongolian-registered legal entities are entitled to hold exploration licenses.

Exploration license holders are also subject to various

environmental protection obligations. Within 30 days of receiving an exploration license, the holder must prepare, and submit to the relevant authorities, an environmental protection and reclamation plan. Once the plan has been approved by the relevant authorities, the holder of the exploration license must deposit funds equal to 50% of its environmental protection budget for that particular year in a bank account established by the governing authority of the *soum* (district) in which the exploration license area is located. Holders of exploration licenses must also submit to relevant authorities an exploration plan and annual reports of exploration activities.

Reserves

Under the 2006 Minerals Law, a mining license holder must extract all of the mineral reserves that are within the license area. The purpose of this provision is to prevent “high-grading”, but the net effect is to mandate mining practices that are not consistent with practices in countries where free-market principles prevail and the concept of mining mineral reserves on an economically viable basis is recognized and understood. It is unclear what consequences, if any, may follow from non-compliance with this provision.

Mining Licenses

If a commercially viable mineral resource is defined within the license area of an exploration license, the holder of the exploration license is entitled to apply for a mining license covering the relevant portion of the license area of the mineral exploration license defined by specified longitude and latitude coordinates. A mining license holder has the right to conduct mining activities throughout the license area and to construct structures within the license area that are related to its mining activities. Mining licenses are granted by the Mineral Resources Authority of Mongolia (MRAM) for an initial term of 30 years and are renewable for two successive twenty-year periods, for a maximum period of 70 years. Upon the expiration of a mining license, the license and the rights under such a license revert to the government of Mongolia. Only Mongolian legal entities are entitled to hold mining licenses. In the case of all minerals other than coal and

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common construction minerals (e.g., sand and gravel), annual license fees of US\$15.00 are payable per hectare of the relevant mining license area. In the case of coal and construction minerals, the per-hectare fee is US\$5.00. A mining license is subject to cancellation if applicable license fees are not paid on time or other requirements of the 2006 Minerals Law or other relevant laws are not complied with. To receive a mining license, an exploration license holder must submit an application to MRAM together with, among other documents, an environmental impact assessment and a resource report. Holders of mining licenses must also prepare environmental protection and reclamation plans and comply with various reporting and security deposit requirements.

Pre-Mining Agreements

After a mineral reserve has been defined and recorded, an exploration license holder may apply to MRAM for a pre-mining agreement. During the term of this agreement, which may not exceed three years, Mongolian-law compliant final feasibility studies must be completed, mine facilities must be developed, and the mine must be brought into production.

Local Government Approval of Exploration Licenses and Mining Licenses

Pursuant to the Mongolian Licensing Law, the granting of each exploration license and mining license by MRAM must be approved by the governor of the *aimag* (province) in which the relevant license area is located. The 2006 Minerals Law also provides that the holder of an exploration license has an exclusive right to obtain a mining license covering all or any relevant portion of the exploration license area.

Approval to Commence Mining Operations

Pursuant to the 2006 Minerals Law, before a mining license holder can bring a mine into production, the Ministry of Mineral Resources and Energy (MMRE) appoints a commission to review and audit pre-mining requirements compliance by the mining license holder that proposes to put a mine into operation. In particular, the commission reviews the license holder's compliance with all pre-mining requirements provided for in the 2006 Minerals Law and reviews the key documents to determine whether they have been prepared in compliance with applicable laws and regulations.

State Participation in Mineral Deposits of Strategic Importance

The 2006 Minerals Law provides that the state is entitled to participate to an extent of up to a 50% equity interest or up to a 34% equity interest, respectively, depending on whether the quantity and grade of a "Mineral Deposit of Strategic Importance" have or have not been defined by exploration deemed to have been funded from the state budget. The terms and conditions of such

participation are subject to negotiation between the government of Mongolia and the license holder and may not necessarily adhere to the 50% or 34% limitations. The Minerals Law does not provide any guidelines as to the form such negotiations should take. The Minerals Law further provides that any company which holds a Mineral Deposit of Strategic Importance is required to list at least 10% of its shares on the Mongolian Stock Exchange.

Investment Agreements

A mining license holder that undertakes to invest more than certain threshold amounts over the first five years of a mining project may apply to the state to enter into an "Investment Agreement" concerning the stability of tax rates, the right to sell products at international market prices, a guarantee that the license holder may receive and dispose of income from such sales at its own discretion, and provisions with respect to the amount and term of the license holder's investment.

The term of each Investment Agreement will depend on the monetary amount of the five year commitment as follows:

Minimum investment (US\$)	Agreement term
50 million	10 years
100 million	15 years
300 million	30 years

Royalties

A royalty at the rate of 5% is payable in respect of the sales price of all products extracted pursuant to a mining license (other than domestically sold coal and construction minerals) that are sold, shipped for sale, or otherwise used.

Mongolian Laws Relating to Additional Permits

Various aspects of mine construction and operation require permits from relevant central and regional governmental authorities. For example, permits must be obtained before proceeding with a general mine development plan and at various stages during the construction of mining facilities and mine start-up. A permit is similarly required for the use of water and for the use of explosives for blasting. In addition, work undertaken pursuant to permits is subject to ongoing review and verification by relevant authorities.

Under the Environmental Protection Law (EPL) of Mongolia, business entities and organizations have the following duties with respect to environmental protection:

- to comply with the EPL and the decisions of the government, local self-governing organizations, local governors and Mongolian state inspectors;
- to comply with environmental standards, limits, legislation and procedures and to supervise their implementation within their organization;
- to keep records on toxic substances, adverse impacts, and waste discharged into the environment; and
- to report on measures taken to reduce or eliminate toxic chemicals, adverse impacts, and waste.

The 2006 Minerals Law also provides for the following administrative sanctions that may be levied against license holders found in violation of environmental protection obligations. The types of sanction are: a fine to the amount of MNT 500,000—1,000,000 (*togros*); and a revocation of the license, with no license to be issued to such a holder for 20 years.

On 16 July 2009, parliament enacted a new law (the “Mining Prohibition in Specified Areas Law”) that prohibits minerals exploration and mining in the following described areas:

- headwaters of rivers and lakes;
- forest areas as defined in the Forest Law of Mongolia; and
- land areas adjacent to rivers and lakes as defined in the Water Law of Mongolia.

The Law on Special Permits to Conduct Business Activities was adopted on 1 February 2001. Under this law, in the case where the terms, conditions and requirements of the license are violated, the initial granting authority may suspend the license for a term of up to three months based on the expert opinion of a professional inspector of the authority. Under Article 14 of the law, a license may be revoked on the following occasions:

- 14.1.1 The license holder requested so.
- 14.1.2 The legal entity has been liquidated.
- 14.1.3 It was determined the documents were falsified when applying for the license.
- 14.1.4 The conditions and the requirements of the license were violated repeatedly or seriously violated.
- 14.1.5 The demands to remedy the violations were not complied with during the suspension period of the license.

Mongolian Laws and Regulations Relating to Labor, Health and Safety

The Mongolian Labour Law (1999) (“Labour Law”) and the Labour Safety and Sanitary Law (2008) (“Labour Safety Law”) contain provisions of general application in relation to labor, health and safety. A mining license holder must carry out activities that ensure: i) safety for the citizens of the relevant *soum* or district; and ii) labor safety and proper sanitary conditions for its employees. The license holder must also submit an annual report on safety to the State Professional Inspection Agency and MRAM. If a license holder is found to have continually violated mining operation safety regulations, its license(s) may be suspended by a state inspector for up to two months, and if the deficiencies are not eliminated within this period, the license(s) may be revoked. If a mining license holder causes serious damage to human health through failure to implement safety rules and appropriate technical standards while using toxic chemicals and substances, its license may be revoked and no new license issued for a period of up to 20 years. Criminal sanctions may also be imposed for violating the health and safety provisions of the 2006 Minerals Law, in extreme cases.

Mongolian Laws and Regulations Relating to Taxation

A summary of the principal tax legislation that may affect the operations of a company in Mongolia is as follows.

- The general income tax rate applicable to business entities with Mongolian source income is 10% on the first MNT 3 billion of taxable income and 25% on amounts in excess thereof.
- A value-added tax at a rate of 10% is payable in respect of all goods sold, work performed and services provided within Mongolia. Value-added tax is also payable in respect of goods imported into Mongolia and in respect of certain service fee payments made by Mongolian taxpayers to non-resident service providers. Pursuant to the Law on Value-Added Tax of Mongolia, VAT shall be at 0% for the exported final products of mining and this law states that the final products of mining shall be determined by government resolution. Therefore the government passed a resolution approving a list of final products consisting of: uranium concentrate, roasted molybdenum concentrate, molybdenum oxide, washed and concentrated coal, briquettes produced from coal and other hard fuel, coal coke and the half coke thereof, brown coal coke and the half coke thereof, and coal tar, etc.
- Equipment and other goods imported into Mongolia are also subject to an import duty, generally at the rate of 5%.
- Mongolian employers are required to withhold income tax and social insurance fees owed by their employees from salaries payable to such employees, and to make an additional employer payment to the Mongolian social insurance fund.
- A company and its subsidiaries will be obligated to make other regular payments which do not fall under the above-noted tax laws of Mongolia. For example, fees will be payable in respect of foreign citizens employed in Mongolia, for the use of water, for lease payments in respect of land surface rights, for environmental bonding obligations (addressed in more detail earlier), for annual mineral license fees and other license renewal fees, for mineral royalties (addressed in more detail earlier), and for annual vehicle taxes.
- Pursuant to the Government Resolution on approving procedures and fixing rates of payment (air payment) No. 273, any legal entities, individuals and organizations shall pay MNT 1 (*togrog*) per kilogram of extracted raw coal, and may change depending on the capacity to harm of the coal in accordance with the appendix of the resolution.

Mongolian Laws Relating to Coal Export Requirements

A Mongolian mining company, holding a valid mining license, has the right to export and sell its coal on the international market. There is no additional export license required. There are, however, certain requirements that

must be complied with and procedures that must be followed in order to lawfully export coal. First, a coal mining company must pay the appropriate royalty and obtain a document evidencing such payment from the relevant tax office. Second, the coal producer/exporter must obtain a certificate of origin from the Mongolian Chamber of Commerce and Industry in respect of each shipment of coal. Finally, the producer/exporter must obtain a certificate from the Mongolian National Centre of Standardization and Metrology certifying that the coal to be shipped is properly classified.

Mongolian Laws and Regulations Relating to Land Tenure

Land tenure in Mongolia is divided into: i) ownership rights; ii) possession rights; and iii) use rights. Only Mongolian citizens can own land. Mongolian citizens, organizations and legal entities that are not deemed to be a business entity with foreign investment (“BEFI”) are entitled to possess land, which entitles them to pledge their interest and to transfer and/or lease it, all subject to approval by relevant authorities. BEFIs may only acquire use rights over land, which may not be transferred, pledged or leased. To engage in mining activities the license holder, if it is a BEFI, must acquire land use rights to the relevant land area. Land use rights can be granted for a period of up to 60 years, although in practice “Land Use Certificates” are typically issued for shorter terms. The Land Law provides that renewals may be made once or more than once, but that the maximum term of any renewal may not exceed a period of 40 years. A mining license holder must enter into either a land possession or land use agreement with relevant land owners, possessors, or the governing authorities of *soums* and districts and obtain a Land Use

Certificate. An exploration license is also not a real property interest and does not convey either land possession or land use rights to the holder. But it is not clear whether an exploration license holder must obtain a Land Use Certificate before conducting minerals exploration activities.

Mongolian Laws Relating to Foreign Investment

Where 25% or more of the paid-in-capital of a Mongolian company is contributed from foreign sources, such a company is deemed to be a BEFI and the company must register with the Foreign Investment and Foreign Trade Agency (FIFTA) and obtain a document certifying the company’s status as a BEFI. In August 2008, Mongolia’s Foreign Investment Law was amended to increase the minimum paid-in capital requirement for BEFIs from the equivalent of US\$10,000 to the equivalent of US\$100,000.

Conclusion

Mongolia’s laws concerning the mining industry are still very young and amendments to the laws are constantly arising and being considered. Even as the author writes on the existing laws and regulations, the government of Mongolia is preparing yet another Mining Law which advances the regulation of the mining sector. Although there are a number of normative and institutional-level issues in Mongolia, the author believes Mongolia has taken substantial steps toward establishing the legal structures that will be able to function as a positive factor in facilitating the development of the country’s mining industry.