MONGOLIA

INVESTMENT CLIMATE STATEMENT

2015

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Executive Summary

Foreign Direct Investment (FDI) into Mongolia has trended downward since its 2011 peak of $4.7 billion. Overall, FDI into Mongolia fell by 85 percent from 2011 through the first quarter of 2015, with $644 million of FDI in 2014. Some 80 percent of FDI into Mongolia annually targets the mining sector and falling global coal and copper prices have dampened investor interest. Mongolia's elected leaders readily accept, however, that government missteps (confiscating selected mining licenses, levying a mining-specific windfall profits tax, assuming veto rights over mining company business decisions, etc.) collectively amounted to a far greater disincentive to investment; these leaders say they recognize the need to correct course.

Parliament's ousting of the Democratic Party-led coalition Government in November 2014 clearly reflected a lack of confidence in the government's economic policies. In December 2014, new Prime Minister Saikhanbileg led an all-party unity government into office vowing to focus its efforts virtually exclusively on Mongolia's battered economy, to make restoration of FDI the center of those efforts, and to put the launching at long last of two FDI-fueled mining mega-projects – OyuTolgoi (copper/gold) and TavanTolgoi (coal) – at the epicenter of efforts. The new PM has so far received high grades from the Mongolian public for sincerity and determination but low grades for results. A sign that the PM and his government mean to turn this situation around is the May 18, 2015, signing of the *Oyu Tolgoi Underground Mine Development and Financing Plan* (Plan) by Rio Tinto and the representatives of the GOM. This plan lays clear steps, with benchmarks, that will allow the parties to move the long-delayed, marquee project forward. The PM's robust and public defense of the Plan before Parliament on May 22 encouraged investors' belief that GOM is now committed to fundamentally changing its attitude toward FDI: That "Mongolia is Open for Business," as the government press releases have stated in the aftermath of the announcement of the Plan. Investors will judge the GOM's resolve to live up to the obligations of its "Open for Business" claims by how it treats investments beyond OT.

As most Mongolian eyes focus on Parliament, international investors have an additional and serious concern – the evident willingness of Mongolian state prosecutors and other authorities to unilaterally impose "exit bans" on foreign business executives whose companies become involved in business-related disputes with the government or individual Mongolian citizens. The 2015 conviction and imprisonment of three mining executives (one of them a U.S. citizen) suggested to investors that Mongolian courts do not fully observe principles of due process, and that foreign investors risk being coerced into settling legal disputes on disadvantageous terms.

In 2014, investors told us that those willing to realistically accept the challenges of Mongolia's commodity-driven economy and rough and tumble political and judicial processes might find profitable medium- to long-term investment opportunities. Mongolia, after all, has some of the world's largest untapped mineral reserves. For U.S. investors, mining and mining-related services represent the most important and potentially remunerative sectors for long-term investment in Mongolia. Other promising sectors include infrastructure, transportation, energy, construction, healthcare, agriculture, tourism, and environmental products and services. But investor concerns about weak rule of law in Mongolia require us to heavily caveat even last year's qualified endorsement.

1. Openness To, and Restrictions Upon, Foreign Investment

Attitude toward Foreign Direct Investment

DISCLAIMER: The Department of State provides the information contained in the Investment Climate Statements solely for our readers' information. Every effort has been made to provide accurate and complete information. However, neither the U.S. Government nor the Department of State guarantees or assumes any legal liability for the accuracy, completeness, or usefulness of any information disclosed in the Investment Climate Statements.

Foreign Direct Investment (FDI) in Mongolia has declined by 85 percent since 2012. Most key elected leaders in Mongolia – including President Ts. Elbegdorj (elected in 2008 and re-elected in 2013), new Prime Minister Saikhanbileg (named in December of 2014) as well as immediate past Prime Minister N. Altankhuyag (in office June 2012 until December 2014), and Parliament Speaker Z Enkhbold (in office June 2012 to present) – have consistently cited Government of Mongolia (GOM) missteps and declining global commodity prices as responsible for the dramatic decline in FDI. In relation to the latter cause, senior officials consistently and publicly state their support for FDI, pledging to correct policies that have negatively impacted FDI. These commitments include adopting more investor-friendly investment and natural resource-related legislation; confirming that the GOM fully intends to keep such foreign investment commitments as the 2009 Oyu Tolgoi Investment Agreement (IA); and most recently, promising to honor international arbitration judgments. One possible sign that GOM stands by these commitments is the May 18 signing of the *Oyu Tolgoi Underground Mine Development and Financing Plan* (hereafter the Plan) by Rio Tinto and the representatives of the GOM. (For a copy of the Plan: http://www.turquoisehill.com/i/pdf/2015-05-18_OTUMDAFP.pdf.) The investor community has explicitly stated that the Plan's clear steps should resolve the lingering, economically crippling dispute with the Rio Tinto Group over the interpretation of the controlling IA as regards development of underground Phase 2 of the Oyu Tolgoi (OT) copper-gold mega mine; and so, demonstrate GOM support for the transparent rule of law, sanctity of contracts, and free market principles, at least for the OT megaproject. However, investors, while praising the Plan and its implications for investment, continue to question if support for FDI at OT will translate into similar commitments for the broader investment climate not covered under the OT IA and the Plan. Other problems, such as the perceived abuse of exit bans, remain unresolved. Innumerable commentators allege that the several official Mongolian entities empowered to level exit bans against individual investors and company executives often do so as a means of coercing foreigners to settle business disputes with the GOM or Mongolian citizens on disadvantageous terms and thereby have made investing and doing business in Mongolia much riskier. Embassy officials have cited exit bans and legal cases as having "significant, detrimental impacts on foreign direct investment."

Other Investment Policy Reviews

UNCTAD Mongolia IPR:
http://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=758.

WTO Mongolia IPR in the context of a Trade Policy Review:
http://www.wto.org/english/tratop_e/tpr_e/tp245_e.htm.

OECD Mongolia IPRs: While OECD has not conducted a full-blown IPR of Mongolia, it has executed numerous economic studies related to investment and development in Mongolia available at http://www.oecd.org/countries/mongolia/.

Laws/Regulations of Foreign Direct Investment

The Investment Law of Mongolia

In October 2013, Parliament passed the Investment Law of Mongolia (IL). Entering into effect on November 1, the IL replaced the controversial 2012 Strategic Entities Foreign Investment Law (SEFIL), which had given the GOM wide discretion in restricting and monitoring foreign investments in sectors and geographic regions the GOM chose to unilaterally pronounce "strategic" even years after investments had been made. Overall, the IL purports to set down legal rights and obligations of investors in Mongolia, stabilizes the tax environment, establishes the powers and responsibilities of the agency that regulates investment, and provides incentives to encourage investment. Foreign investors are given the same protections as domestic investors.

Domestic vs. Foreign: It's Where You Are, Not Who You Are

Unlike SEFIL, what distinguishes a foreign from a domestic investor in the IL is not nationality but where the investor resides. A foreigner who resides permanently in Mongolia may be considered a domestic investor for purposes of the law while a Mongolian who lives abroad permanently may be considered a foreign investor. Investment may be made in any sector not prohibited or restricted by law. (Note: For example, neither foreign nor domestic investors may invest in casinos, horse racing, or other gaming activities, all of which are specifically restricted by law.) Accordingly, investments by private individuals or firms are no longer subject to special approval other than registration with the State Registration Office (SRO), which simplifies the procedures for doing business, unless sector-specific legislation mandates additional requirements. IL offers U.S. investor residing in Mongolia and who opts to register his or her company in Mongolia the opportunity to receive national treatment. U.S. investors, who choose not to register their companies in Mongolia, may also qualify for national treatment under the terms of the U.S.-Mongolia Bilateral Investment Treaty or BIT.

Attempt to Create Greater Tax Certainty

A central feature of IL promoted by the GOM is the tax incentives in the form of tax stabilization certificates. New projects and some older projects that meet requirements may qualify for favorable tax treatment for periods up to 27 years. Affected taxes may include corporate income tax, customs duties, value-added tax, and mineral resource royalties. The determining criteria for participation in the incentive program tax stabilization is the amount of investment, the sector involved, and the geographical area involved. Some legal commentators predict that limitations on the transferability of the new certificates will complicate and eventually stifle investment.

The Invest Mongolia Agency

IL created a new investment promotion entity, the Invest Mongolia Agency (IMA), which reports to the Office of the Prime Minister, to replace the Foreign Investment Regulation and Registration Department (FIRRD). IMA is responsible for issuing the tax stabilization certificates. To contact IMA go to www.investmongolia.com. The State Registration Office (SRO) is responsible for registering companies and investors: http://www.burtgel.mn/.

Industrial Promotion

December 2014 saw the creation of a new government and with it, a new Ministry of Industry (MOI), carved out from the former Ministry of Industry and Food and Agriculture. Parliament has charged MOI with creating and implementing an industrial policy for Mongolia aimed at promoting value-added production in non-agricultural sectors, including but not limited to minerals and metals processing, construction materials production, plastic and chemical production, and hydrocarbon refining. The newly minted Ministry of Food and Agriculture is responsible for value-added production in the food production and livestock sectors.

MOI officials describe the ministry's overall goal as that of import substitution, to be accomplished by employing state funds, as yet undefined tax preferences for domestic production, and import tariffs. Parliament is expected to consider specific policies that promote industrialization during its Spring 2015 session. Investors may be expected to carefully watch to see that any such policies are clear and business-friendly.

Limits on Foreign Control

Generally, foreign and domestic businesses can establish and engage in any form of business activity on an equal footing. The U.S.-Mongolia Bi-lateral Investment Treaty (BIT: http://www.state.gov/documents/organization/43579.pdf) expressly extends to U.S. investors the benefits of national treatment in Mongolia with exceptions in the banking and finance and real estate sectors. In addition, the 2013 Investment Law of Mongolia (IL) guarantees that all foreign companies and investors registered with the Invest Mongolia Agency are to be treated as Mongolian-registered entities and subject to the same rights and obligations related to ownership and establishment pertaining to any Mongolian entity. (For information on IL see 1.3.)

Although Mongolia imposes no general legal restrictions on foreign project financing or the formation of joint ventures or other business partnerships, the GOM sometimes imposes specific restrictions on an ad hoc, project-by-project basis. These restrictive covenants are most likely be imposed in sectors in which the GOM determines investment may have an impact on national security concerns—e.g., the mining sector. Hence international bidders responding to the third tender for development and operation rights connected to the Tavan Tolgoi (TT) coal mining project were required to find local implementing partners. Local legal experts note that the system by which the GOM regulates such transactions lacks clear statutory bases and transparent, predictable regulatory procedures.

Privatization Program

In mid-2014, President Elbegdorj of Mongolia declared that the GOM should divest itself of many of its state-owned entities in order to streamline government and improve the operations of these entities by subjecting them to market discipline – an approach he calls "Smart Government." His call has been taken up by the current government, which is seeking to legislate a framework for the full or partial privatization of some parts of state-owned enterprises; for example, the government has proposed privatizing up to 49% of the state-owned airline MIAT —or all of the government's holdings in the case of state-owned real estate in Mongolia's urban centers. The GOM has welcomed foreign participation in those efforts but has

not yet clearly articulated how the tendering process will work. On the contrary, the GOM has continued to create new state-owned entities.

Screening of FDI

Mongolia has no formal system for screening investments as such, although businesses report a passive system in which specific investments, which are otherwise legal but which the GOM at different levels does not really want, may face steady resistance to registration, permitting, etc.

Although local legal experts dispute its constitutional and statutory authority to limit or suspend legally authorized use rights, the National Security Council of Mongolia (NCSM) has asserted the power to do so, which can and has affected FDI in Mongolia's mining sector. In 2010, the President of Mongolia used his authority as head of the NSCM to suspend the issuance and processing of both mining and exploration licenses. He argued that the flaws of the licensing regime constituted a threat to national security that justified the NSCM suspending issuances. Domestic and foreign investors and Mongolian government officials disputed this moratorium, claiming that neither the President nor the NCSM had constitutional or statutory authority to supersede the government's regulatory authority over mining. In 2014 parliament revoked the moratorium. The NSCM also issues assessments of public and private projects of national interest. Barring parliamentary action, a positive assessment allows a project to move forward, while a negative one effectively cancels the project. Investors are concerned that a precedent has been created that will allow future security councils to subject proposed investments to the same kind of secretive, constitutionally dubious national security reviews.

Competition Law

Mongolia's Agency for Fair Competition and Consumer Protection (AFCCP: http://www.afccp.gov.mn/) reviews domestic transactions for competition related concerns. For a description of the AFCCP and its legal and regulatory powers see http://unctad.org/en/PublicationsLibrary/ditcclp2012d2_Mongolia_en.pdf.

Investment Trends

Investor Concerns over Travel Bans

Investors and local legal experts have grown to fear what they call the capricious and arbitrary use of travel bans by Mongolian officials, sometimes at the behest of private interests, as a means to coerce foreign investors to settle civil and criminal disputes. Immigration officials may impose a travel ban for a variety of reasons, including an individual's involvement in civil disputes, pending criminal investigations, or for immigration violations. If banned for either a civil or criminal dispute, exit will not be allowed until either the dispute is resolved administratively or a court renders and implements a judgment. Neither current law nor regulation establishes a transparent process or clear time-table for settlement of such issues. Resolution of criminal and civil commercial cases has taken up to 2.5 years during which time the foreign citizen must remain in Mongolia.

The recent experience of three foreign nationals (among them an American executive), detained

for over 2.5 years under these exit ban provisions and ultimately convicted (but later pardoned), in a trial that both international and Mongolian observers—Including the President, Speaker of Parliament, and the Prime Minister of Mongolia—called procedurally flawed, has generated fear among investors that they will be indefinitely detained and may be ultimately incarcerated for such civil matters as contract and tax disputes.

2006 Minerals Law Amended

In July 1, 2014, Parliament amended the 2006 Minerals Law. The GOM presented the 2014 amendments as the last changes to the law for the next 5 to 10 years, but investors continue to worry that the GOM will fiddle with it without giving the amendments a chance to work. Investors have praised the GOM and Parliament for consulting with stakeholders while drafting the law; however, concerns remain. The amendments do not clearly delineate, for example, whether localities may delay or entirely veto exploration and mining activities in their jurisdictions after the central government has issued appropriate licenses.

Oyu Tolgoi *Plan* Offers a Path Forward

Domestic and foreign investors tell us (and we agree with their assessments) that the *Oyu Tolgoi Underground Mine Development and Financing Plan* (hereafter the Plan) dramatically improves the perception of Mongolia as an investment destination, serious concerns about exit bans, corruption, lack of transparency and the rule of law notwithstanding.

In October 2009, the GOM, Ivanhoe Mines of Canada, and the Rio Tinto Group's U.S.-based Copper Division negotiated investment and share-holders agreements for the Oyu Tolgoi (OT) copper-gold deposit located in Mongolia's South Gobi desert. Rio Tinto eventually acquired control of Ivanhoe, renaming it Turquoise Hill Resources (TRQ). The OT agreements vest the government of Mongolia with 34% of the project and TRQ with 66%, and provide guarantees for local employment and procurement. OT formally commenced operations and exports of copper-gold concentrate in mid-2013.

Investors had hoped that the export of copper and gold would lead to approval of a project finance agreement for Phase II, which is to be an underground block-cave mine and which is expected to account for 80 % of OT's full value over its 40-year plus mine-life. However, from 2013 through 2014, both Rio Tinto and the GOM had failed to agree on key issues related to project costs, management fees, taxation, and permitting, among other issues. This mutual inability to reach agreement had effectively halted Phase II financing.

The domestic impact of the impasse trimmed over 2000 jobs and the planned procurement purchases related to Phase II. For the GOM, this trimming represented a substantial loss of revenue of between US $200 to US $300 million per year from the state budget. For the people of Mongolia, these cuts meant that employees and contractors have not developed the skills needed to run OT and other mining developments, in addition the impact on vitally needed household income.

Spelling out the particular and mutual obligations of each party, the Plan sets out a series of confidence building steps between Rio Tinto and the GOM in areas of taxation, local procurement, local development, permitting, etc, which create a path forward to restarting Phase II. Regarding revenues, the Plan reaffirms earlier commitments that 53% of the project value to go to Mongolia over the life of OT; and estimates that the next seven years of Phase II will see direct payments to the GOM of approximately US $300 million per year, with overall spend in Mongolia reaching approximately of US $1.3 billion annually. For more details of the Plan: http://www.turquoisehill.com/i/pdf/2015-05-18_OTUMDAFP.pdf.

For foreign investors the importance of this settlement cannot be overestimated. From inception, OT has embodied both the positive and negative of Mongolia's investment climate. Negatively, the dispute raised doubts about the GOM's commitment to contract sanctity, which certainly become a factor in the downgrading of Mongolia's sovereign credit ratings, and has been blamed for the economy-crippling drop in FDI since 2012. Positively, investors perceive that OT settlement proves that Mongolia can say "Yes" to key projects undertaken with foreign involvement and investment; and demonstrates GOM willingness to amend laws and regulations to enhance and ensure the commercial viability of mining projects. Investors emphatically state that resolution of this dispute may spur a renaissance for FDI akin to the earlier high GDP growth years of 2010-2012, although they caveat this hope by noting that improvements in other areas of investment climate discussed in this report must parallel the justly praised OT settlement.

Table 1

Measure	Year	Index or Rank	Website Address
TI Corruption Perceptions index	2014	80 of 175	transparency.org/cpi2014/results
World Bank's Doing Business Report "Ease of Doing Business"	2015	72 of 189	doingbusiness.org/rankings
Global Innovation Index	2014	56 of 143	globalinnovationindex.org/content.aspx?page=data-analysis
World Bank GNI per capita	2013	3,770	data.worldbank.org/indicator/NY.GNP.PCAP.CD

Millennium Challenge Corporation Country Scorecard

The Millennium Challenge Corporation, a U.S. Government entity charged with delivering development grants to countries that have demonstrated a commitment to reform, produced scorecards for countries with a per capita gross national income (GNI) or $4,125 or less. A list of countries/economies with MCC scorecards and links to those scorecards is available here: http://www.mcc.gov/pages/selection/scorecards. Details on each of the MCC's indicators and a guide to reading the scorecards are available here: http://www.mcc.gov/pages/docs/doc/report-guide-to-the-indicators-and-the-selection-process-fy-2015. Mongolia was selected for second

MCC compact in December 2015.

2. Conversion and Transfer Policies

Foreign Exchange

The Mongolian government employs a liberal regime for controlling foreign exchange for investment remittances. Foreign and domestic businesses report no problems converting or transferring investment funds, profits and revenues, loan repayments, or lease payments into whatever currency they wish to wherever they wish. There remains no difficulty in obtaining foreign exchange in virtually any major world currency. Mongolia's currency is fully convertible for a wide array of international currencies and does fluctuate regularly in response to economic trends. In regards to domestic transactions, current law requires all domestic transactions be conducted in Mongolia's national currency, the Tugrik (MNT), except entities granted limited waivers for non-Tugrik transactions by Mongolia's central bank, the Bank of Mongolia (BOM).

Remittance Policies

Businesses report no delays in remitting investment returns or receiving in-bound funds. Most transfers occur within 1-2 business days or, at most, a single business week. However, in response to occasional currency shortages, most often of U.S. dollars, commercial banks can temporally limit the amounts they daily exchange, transmit abroad, or allow to be withdrawn.

Ease of transfer aside, foreign investors sometimes criticize Mongolia's lack of sophisticated mechanisms for converting currencies and hedging forward exposure to MNT. Many Mongolian financial institutions lack experience with these arrangements. Moreover, Mongolian banking law currently provides incomplete statutory grounds and regulatory support for such activity. Letters of credit remain difficult to obtain; and the government has sometimes resorted to pay for goods and services rendered under domestic government contracts with promissory notes, which cannot be directly exchanged into other currencies. The immediate impact has been to limit access to certain types of foreign capital, as international companies resist parking cash in Mongolian banks or in local debt instruments.

As of June 2014, Mongolia complied with the Financial Action Task Force (FATF) requirements related to money laundering and terrorist financing (AML/CTF). For Mongolia's status, see http://www.fatf-gafi.org/countries/j-m/mongolia/documents/fatf-compliance-june-2014.html.

3. Expropriation and Compensation

Mongolia has generally respected property rights for most asset types. However, investors have expressed concern over actions that they believe represent either "creeping expropriation" or more direct expropriation, especially but not exclusively those associated with the resource extraction sector.

Security of Ownership

The U.S.-Mongolia Bilateral Investment Treaty (BIT) entered in force in 1997. Under this BIT (http://www.state.gov/documents/organization/43579.pdf), Mongolia and the United States have agreed to international law standards for expropriation and compensation for expropriation. In addition, both Mongolia's laws and constitution recognize private property rights and the rights associated with their use, and specifically bar the government from expropriating such assets. To date, the GOM has been accused of only a single act of expropriation against an American-owned mining asset.

The Mongolian government may exercise eminent domain in the national interest. Under the current land law, Mongolian state entities at all levels can claim land or modify use rights for purposes of economic development, national security, historical preservation, and environmental and rangeland protection. Investors have expressed little disagreement with such takings in principle; but worry that the lack of clear lines of authority among the central, provincial, and municipal levels of government can lead to a loss of property rights. For example, the 2006 Minerals Law (as amended in 2014) still provides no clear limit on provincial control of permits and special use rights; or guidance on how to apply these powers beyond codifying that the provincial and local authorities have some authority over activities occurring in their *aimags* (provinces) and *soums* (counties). Faced with these unclear lines of authority, the central government often interprets the rules and regulations differently from the provincial and municipal authorities but declines to enforce its interpretation or even to assist in mediating among the disputing parties, all of which can, and has, effectively suspend investors' access to property and licensed use rights for months and years. The GOM acknowledges the problem but has taken no steps to resolve it.

The Use of Criminal Courts to Invalidate Use Rights

Recently, investors have vehemently criticized the revocation of economic rights by Mongolia's criminal courts. For example, in 2013 a criminal court judge revoked 106 mining licenses, because these had been granted during the tenure of an official subsequently found criminally guilty of corruption. At no time did the court offer specific evidence proving that these licenses, among the hundreds granted during the official's term, were improperly granted. Calling this a form of judicial expropriation, local legal experts claim that this action has become more common since 2013, with criminal courts assessing substantial fines from, or revoking rights of, companies – termed civil defendants under Mongolian law – based on third-party corruption convictions. Of the cases we have observed in actual hearings, at no time did the criminal court allow these civil defendants any opportunity to defend themselves before the court during the trial or at hearings specifically focused on proving corporate malfeasance. Local legal experts have noted that Mongolian law and regulation do not allow criminal courts to render administrative decisions on the status of use rights or assess taxes and fees owed, which is the formal statutory province of the Administrative Court of Mongolia. However, experts explain that the administrators find themselves in a bind, as they are obliged to act on court orders, without regard whether the criminal court that issued the order has the authority to do so. Until this gray area of judicial authority is resolved, investors can have had their economic rights expropriated by a part of the judiciary acting outside its remit, without any opportunity to appeal these losses to a proper authority.

4. Dispute Settlement

Legal System, Specialized Courts, Judicial Independence, Judgments of Foreign Courts

Mongolia has adopted the Civil Law tradition in that its courts may informally consider case precedent but are not bound to follow it. Mongolian legal codes and regulations, however, generally lack the specificity of more mature Civil Law systems and this shortcoming often leaves courts attempting to reconcile broadly written codes with the facts of the specific cases they are adjudicating. Although experienced and dedicated judges make due and deliver at least rough justice in routine matters, the lack of guidance for Mongolia's underfinanced and understaffed judicial system invites corruption, especially in cases in which serious money is at stake as in, to take one recurring example, cases pitting large foreign corporations against a domestic government agency or well-connected private Mongolian citizen.

Scholars note in Mongolian legal codes pronounced German and Russian influences and, more recently, influences from the United Kingdom, Canada, and the United States. Mongolia has adopted laws on specific aspects of commerce – including licensing, access to finance, the tax treatment of different types of investment. However, after 25 years of legislating, the passage of new laws and the promulgation of new regulations on contracts, investment, corporate structures, leasing, banking, etc., remains vitally necessary. Enforcement of court judgments related to commerce is apparently a low priority of the implementing agency (the General Executive Agency for Court Decisions, GEACD). The prioritization of creditor claims can be particularly problematic. Foreign judgments are in principle enforceable in Mongolia, though the weak and convoluted system of enforcement of even domestic judgments remains difficult for foreign litigants to navigate.

Bankruptcy

Mongolian law mandates the registration of mortgages and other debt instruments backed by real estate or other immovable collateral. Registration, however, is complicated and slow and the GEACD has scant expertise in evaluating property and seems particularly reluctant to implement eviction notices and collection actions. The enforcement of foreclosure provisions of debt instruments backed by pledges of movable collateral such as licenses and receivables is complicated by the additional Mongolian reality that pledges of moveable property are not centrally registered, a reality that makes very difficult the performance of due diligence from outside Mongolia. Foreign creditors looking to enforce lien rights backed by moveable assets are sometimes surprised to learn only in a bankruptcy proceeding that collateral pledged to them may not be fully owned by the mortgagee or may be also encumbered by a domestic mortgage which, if it predates the agreement they wish to enforce, may take priority over their claim. In brief, bankruptcy and foreclosure is an option on paper, but we can offer no example of a successful bankruptcy process. Indeed, local law firms hold that the bankruptcy process is too vague, onerous, and time consuming to make it a practical step to end a business.

Overall, the legal system does recognize the concept of collateralized assets as security for loans, investment capital, and other debt-based financial mechanisms; and provides for foreclosure, but only through the judicial rather than administrative proceedings. Although a system exists to register immovable property—structures and real estate—for the purpose of confirming

ownership, the current system does not record existing liens against immovable property with inconsistent or non-existent registration of collateral pledges a prime area of confusion. Nor does a system currently exist to register ownership of, and liens on, movable property. Consequently, lenders face the added risk that assets may have already been pledged as security for another debt.

Investment Disputes

There are no hard figures for the number of investment disputes involving foreigners in Mongolia. Most foreign investors desiring to do long-term business in Mongolia prefer to quietly pursue or even abandon particular claims, especially if the government has an interest in the matter, for fear of jeopardizing future opportunities. Strong anecdotal evidence suggests that some Mongolian officials from each branch of government have solicited or offered bribes as a means of pre-empting or resolving particular investment disputes with foreign interests.

In cases in which the government, at whatever level, is involved directly or indirectly, in a dispute, investors have reported and we have observed substantial government interference in the dispute resolution process, both administrative and judicial. Foreign investors describe three general categories of disputes that invite such interference. The first category comprises disputes between private parties that involve one or more Mongolian government agencies. In these cases, a Mongolian party may exploit contacts in government, the judiciary, law enforcement, or prosecutor's office to coerce a foreign party to accede to some demand. The second category involves disputes between investors and the government directly. In these cases, the government may claim a sovereign right to intervene in the involved business venture, often because the government itself is operating a competing state-owned entity or because particular officials have undisclosed business interests. The third category involves a Mongolian tax official or prosecutor levying highly inflated tax assessments against a foreign entity and demanding immediate payment, sometimes in concert with imposition of exit bans on particular company executives or even the filing of criminal charges. (See Chapter 1.9 for details on travel bans.)

International Arbitration

The GOM consistently declares it will honor resulting arbitral awards. In March 2015, an international arbitral tribunal awarded the Canadian uranium mining company Khan Resources just over US $100 million as compensation from the Government of Mongolia for the government's expropriation of Khan Resources' legally granted mining rights. Talks between the GOM and Khan Resources over payment have stalled. In late April, the Minister of Justice and Home Affairs publically stated that Mongolia will seek to nullify the binding judgment of the arbitral court. This repudiation of the arbitral decision has given rise to investor concerns that Mongolia will not honor promises to investors on other obligations.

Mongolian businesses partnered with foreign investors often will accept international arbitration, as do government agencies that contract business with foreign investors, rather than avail themselves of the Mongolian Arbitration Bureau operated by the Mongolian National Chamber of Commerce and Industry. Foreign investors tell us that they prefer international arbitration, because they perceive domestic arbitrators as too politicized, too unfamiliar with commercial practices, and too self-interested to render fair decisions.

The U.S.-Mongolia Bilateral Investment Treaty (BIT) entitles both U.S. and Mongolian investors to seek international arbitration in the case of investor-state disputes. (For the BIT: http://www.state.gov/documents/organization/43579.pdf.)

ICSID Convention and New York Convention

Mongolia ratified the Washington Convention and joined the International Centre for Settlement of Investment Disputes in 1991. It also signed and ratified the New York Convention in 1994. To our knowledge, the government of Mongolia has accepted international arbitration in several disputes.

Duration of Dispute Resolution

It is hard to say how long it will "typically" take to resolve an investment dispute in Mongolia. Some cases have been settled within a week through quiet discussion among the parties, while others, particularly in the mining sector, have yet to be settled after six years. For disputes arising through loan default or bankruptcy, waits of up to 36 months for final liquidations and settlement of security are not uncommon.

Although arbitration is widely accepted among business people and elements of the government, support for binding international arbitration has not penetrated local Mongolian agencies responsible for executing judgments. Investors routinely report that the most common problem preventing resolution of debt-driven disputes is that the GEACD often resists executing collection orders and court-ordered foreclosures.

5. Performance Requirements and Investment Incentives

WTO/TRIMS

There have been no documented reports or claims that Mongolia employs measures inconsistent with World Trade Organization Trade Related Investment Measures (TRIMS) requirements.

Investment Incentives

The GOM attempts to limit both tax exemptions and incentives, but tries to ensure that tax preferences offered are available to both foreign and domestic investors. The GOM occasionally grants tax exemptions for imports of essential fuel and food products; or for imports in certain sectors targeted for growth, such as the agriculture sector. Such exemptions can apply to both import duties and Mongolia's value-added tax (VAT). In addition, the GOM occasionally extends a 10% tax credit on a case-by-case basis to investments in such key sectors as mining, agriculture, and infrastructure. Under the 2013 Investment Law (IL), foreign-invested companies properly registered and paying taxes in Mongolia are considered domestic-Mongolian entities, thus qualifying for investment incentive packages that, among other incentives, include tax stabilization for a period of years. (For details on the IL see Chapter 1.) In 2014, parliament authorized the Bank of Mongolia (BOM), the central bank, to waive 7.5% of the 10% royalty

payments that gold miners must pay when selling gold to the Bank of Mongolia and Mongolian commercial banks; the transactions must be done in Mongolia's currency, the tugrik.

Research and Development

The Government of Mongolia has limited budgets for research activities, and is quite open to foreign participation, especially in the mining, construction, and agricultural sectors.

Performance Requirements

Restrictions on hiring expatriate labor aside, foreign investors currently need not use local goods, services, or equity; or engage in substitution of imports. The government applies the same geographical restrictions to both foreign and domestic investors. Existing restrictions involve border security, environmental concerns, or local use rights. There are no onerous or discriminatory visas, residence, or work permits requirements imposed on American investors. Neither foreign nor domestic businesses need purchase from local sources or export a certain percentage of output; or require foreign exchange to cover their exports.
The GOM encourages value-added production and local sourcing of human and material inputs in Mongolia, especially for firms engaged in natural resource extraction. Although the GOM has passed no laws forcing local sourcing, government plans call for increased investment in businesses and activities that keep the "value" of a resource in Mongolia. Consequently, companies should expect the GOM to press aggressively for domestic value-added processing. The 2014 Amendments to the 2006 Minerals law of Mongolia have imposed new mandates for local sourcing on mining companies in Mongolia. Specifically, holders of mining licenses should, whenever possible, preferentially supply extracted minerals to Mongolian processing facilities at market prices; should procure goods and services and hire subcontractors from business entities registered in Mongolia; and should ensure that 90 % of workers on site are Mongolian. However, the amendments do not define how "market prices" are to be determined; and implementation of local processing, procurement, and labor requirements may be impractical in many instances. Foreign suppliers registered as Mongolian domestic companies under terms of the IL would satisfy the new local sourcing requirements. (See Chapter 1.3 on the IL.)

Pressure to source locally notwithstanding, foreign investors generally set their own export and production targets without concern for government imposed targets or requirements. There is no requirement to transfer technology. As a matter of law, the government generally imposes no offset requirements for major procurements. Certain tenders and projects on strategic mineral deposits may require agreeing to specific levels of local employment, procurement, or to fund certain facilities or training opportunities as a condition of the tender or project; but as matter of course such conditions are not the normal approach of the government in its tendering and procurement policies. Investors, not the Mongolian government, make arrangements regarding technology, intellectual property, and similar resources and may generally finance as they see fit. Except for a currently unenforced provision of the recently amended Minerals Law of Mongolia requiring mining companies to list 10% of the shares of the Mongolian mining company on the Mongolian Stock exchange, foreign invested businesses currently need sell no shares to Mongolian nationals. Equity stakes are generally at the complete discretion of investors, Mongolian or foreign.

Although Mongolia has no statutory or regulatory requirement, the GOM sometimes restricts the sort of financing that foreign investors may obtain and with whom investors might partner or to whom they might sell shares or equity stakes. These restrictive covenants will most likely be imposed in certain sectors where the investment is determined to have national impact or national security concerns—i.e., the mining sector. Investors and local legal experts note that the system by which the GOM regulates these transactions lacks a clear statutory basis and transparent, predictable regulatory procedures.

Regarding employment, investors can locate and hire workers without using hiring agencies—as long as hiring practices follow Mongolian labor law. Mongolian law requires companies to employ Mongolian workers in certain labor categories whenever a Mongolian can perform the task as well as a foreigner. This law generally applies to unskilled labor categories and not areas where a high degree of technical expertise not existing in Mongolia is required.

Data Storage

The GOM has no forced localization policy for data storage; no legal requirements for IT providers to turn over source code or to provide access for surveillance; and no rules or mechanisms for maintaining a certain amount of data storage at facilities within the territory of Mongolia.

6. Right to Private Ownership and Establishment

Generally, unless otherwise forbidden by law, foreign and domestic businesses can establish and engage in any form of business activity. Under the U.S.-Mongolia Bilateral Investment Treaty (BIT: http://www.state.gov/documents/organization/43579.pdf), U.S. investors receive national treatment in Mongolia and can start up, buy, sell, merge; in short, do whatever they wish with their assets and firms, with exceptions in the banking and finance and real estate sectors, which are carved out for restrictive treatment under the BIT. In addition, the 2013 Investment Law of Mongolia (IL) guarantees that all foreign investors satisfying formal criteria are to be treated as Mongolian-registered entities and subject to the same rights and obligations related to ownership and establishment pertaining to any Mongolian entity. (See Chapter 1.3 for IL.)

7. Protection of Property Rights

Real Property

Mongolia recognizes the right to own private property, movable and immovable. Regardless of nationality, owners can generally do as they wish with their property, except for real estate, ownership of which allows Mongolian citizens to acquire land only in municipalities. (Note: Mongolian domestic companies do not qualify as citizens for the purpose of owning real estate.) Most of Mongolia's non-urban land, such as pasturage or mineral deposits, remains the property of the state, for which foreign and domestic investors may obtain use rights for terms varying from 3 to 90 years, depending on the purpose and relevant legislation. Although no formal law exists allowing Mongolia's pastoral nomadic herders exclusive rights of pasturage and control of water and land rights as such, rural municipalities administering these resources unofficially recognize that traditional, customary access to these resources by pastoralists must be taken into

account before, during, and after other non-resident users, particularly but not exclusively those in the mining sector, access their use and ownership rights. That aside, one can sell, transfer, or securitize structures, shares, use-rights, companies, and movable property, subject to relevant legislation and related regulation controlling such activities. Mongolian law does allow creditors to recover debts by seizing and disposing of property offered as collateral.

Mongolia's Current Regime to Protect Creditors

Investors tell us that Mongolian law can protect creditors but needs reform; and assert that while courts recognize property rights in concept, they have a checkered record of protecting them in practice. Part of the problem is ignorance of, and inexperience with, best international best practices regarding use- rights, land, leases, buildings, and mortgages. As noted in Chapter 4, some judges, whether out of ignorance or apparent partiality for Mongolian disputants over foreigners, fail to follow such practices. Investors tell us that newly trained judges make good faith efforts to uphold property rights but need more experience adjudicating such cases. The legal system also requires judicial foreclosure for any contested foreclosure action. Because all contested foreclosure actions require court review and are subject to appeals up to the Supreme Court of Mongolia, final resolution can take up to 36 months. In addition, creditors report that it's often easier to get than to execute a court ruling. The problem remains inconsistent enforcement. The court orders the State Collection Office (SCO) to seize forfeited assets, which it should then distributes to creditors. However, foreign and domestic investors routinely claim that SCO regularly fails to execute its responsibilities. In addition, nascent systems for determining title and liens and for collecting on debts make lending on local collateral risky. Although a system exists to register immovable property—structures and real estate—for the purpose of confirming ownership, it does not record existing liens; nor does the system record ownership and liens on movable property. Consequently, creditors risk lending on collateral that debtors may not actually own or which may have already been offered as security for other debts.

Intellectual Property Rights

Mongolia supports intellectual property rights (IPR) in general. A member of the World Intellectual Property Organization (WIPO), Mongolia has signed and ratified most relevant treaties and conventions, including the World Trade Organization Agreement on Trade Related Aspects of Intellectual Property Rights (WTO TRIPS). However, Mongolia's parliament has yet to ratify the WIPO Internet treaties. (WIPO: http://www.wipo.int/directory/en/.) Despite this, the Mongolian government and its intellectual property rights enforcer, the Intellectual Property Office of Mongolia (IPOM: http://www.ipom.mn/), make a good faith effort to comply with these agreements.

Under TRIPS and Mongolian law, the Mongolian Customs Authority (MCA) and the National Police (NP) also have an obligation to protect IPR. MCA can seize shipments at the border. The NP has the exclusive power to conduct criminal investigations and bring criminal charges against IPR pirates. The IPOM has the administrative authority to investigate and seize pirated goods administratively. Of these three, the IPOM makes the most consistent efforts to fulfill Mongolia's treaty commitments.

The IPOM generally has an excellent record of protecting American trademarks, copyrights, and patents; however, tight resources limit the IPOM's ability to act. In most cases, when the U.S. Embassy in Ulaanbaatar conveys a complaint from a rights holder to the IPOM, it quickly investigates the complaint. If it judges that an abuse has occurred, it will (and has in every case, so far) seize the pirated products, under administrative powers granted under Mongolian law. We note two areas where enforcement lags. Legitimate software products remain rare in Mongolia, with the IPOM estimating that 95% of the market uses pirated software. The IPOM enforces the law where it can but the scale of the problem dwarfs its capacity to deal with it. Pirated optical media are also readily available and subject to spotty anti-piracy enforcement. The growth of online downloads of pirated optical media by individuals and local Mongolian TV stations effectively eclipsed local production and imports of fake CD's, videos, or DVD's. The IPOM acknowledges that most of these local public and privately held TV stations, some 184 at latest count, regularly broadcast pirated materials; however, the IPOM hesitates to move on these broadcasters, most of which are connected to major government or political figures. The IPOM will act on specific complaints, but will rarely initiate action. For additional information about treaty obligations and points of contact at local IP offices, please see WIPO's country profiles at http://www.wipo.int/directory/en.

Resources for Rights Holders

Contact at the U.S. Embassy in Ulaanbaatar: http://mongolia.usembassy.gov/
NAME: Economic and Commercial Section
TELEPHONE NUMBER: +976-7007-6001
EMAIL ADDRESS: Ulaanbaatar-Econ-Comm@state.gov

For additional resources on protecting IPR in Mongolia, reach out to the American Chamber of Commerce in Mongolia at http://amcham.mn/. The U.S. Embassy also provides a list of attorneys at http://mongolia.usembassy.gov/lawyer_list.html.

8. Transparency of the Regulatory System

In 2011, Parliament passed the Law on Information Transparency and the Right to Information (LIT). LIT sets out which government, legislative, and non-governmental organizations must provide information to the public—both in terms of what information entities should disseminate and how these respective organizations should respond to requests for information by citizens and legal entities residing in Mongolia. The LIT requires that state policies, some legislative acts, and administrative decisions be posted on the appropriate government websites in understandable language for no less than 30 days for comment and review prior to enactment. Comments may be incorporated into proposals if appropriate. In addition, government entities must post public hiring processes, concessions, procurement, and budget and finance information. The LIT specifically exempts the armed services, the border protection and internal troops, and intelligence organizations from its provisions. Ongoing citizen complaints and petitions are not subject to the LIT's provisions; nor does the law apply to intellectual property information, proprietary business information, or personal information. To implement the LIT, the Cabinet of Ministers requires ministries to post proposed regulatory changes on ministerial websites for comment and review at least thirty (30) days before approval. The Cabinet does not specify a standard process for collecting and acting upon public comment and review.

In addition to the LIT, the Law on Making Laws (LML) requires (or requests in the case of parliament) those drafting and submitting laws to parliament—termed lawmakers in the LML—subject their legislative acts to comment and review. Specifically, the President and the ministries must submit legislation for review and comment. Parliament may solicit comment and review but is not required to do so. The LML does not specify who is to be consulted; how they are to be consulted; when or where; and what is to be done with these critiques of legislation. Such nods to transparency notwithstanding, investors find that the current process allows no statutory, systematic, and transparent review of legislation and regulations by stakeholders. Most ministerial initiatives still seem to go unpublished until the draft passes out of a given ministry to the full Cabinet. Typically, the full Cabinet discusses and passes bills on to Parliament, without public input or consultation. Parliament itself neither issues a formal calendar nor routinely announces or opens its standing committees or full chamber hearings to the public. While Parliament at the beginning of each session announces a list of bills to be considered during the session, this list is very general and often amended. New legislation is commonly introduced, discussed, and passed without public announcement or consideration, often rather hastily.

Informal Legislative and Regulatory Processes that Impede FDI

While foreign investors are most often invited by government agencies, NGOs, and industry associations to consult on an ad hoc basis on proposed laws and regulations affecting investments, they are strongly discouraged from taking any public role in such consultations. While this approach may avoid some of the controversies attending public comment by foreign investors, it also makes delivery of their advice less transparent and effectively unofficial, allowing the advice to be ignored by officials and Mongolian NGO's and industry associations.

United States and Mongolia Sign Bilateral Transparency Agreement in 2013

On September 24, 2013, the United States of America and Mongolia signed an Agreement on Transparency in Matters Related to International Trade and Investment (TA). The agreement, signed by United States Trade Representative (USTR) Michael Froman and former Mongolian Foreign Minister Luvsanvandan Bold, marks an important step in developing and broadening the economic relationship between Mongolia and the United States. The goal of the TA is to make it easier for American and Mongolian firms to do business. The agreement covers transparency in the formation of trade-related laws and regulations, the conduct of fair administrative proceedings, and measures to address bribery and corruption. In addition, it provides for commercial laws and regulations to be published in English, making it easier for international investors to operate in Mongolia. In December 2014 the Mongolian parliament ratified the TA, thus sending an unambiguous signal to foreign and domestic businesses that Mongolia seeks to restore confidence in the statutory and regulatory processes affecting commerce and trade in Mongolia. Although ratified, the TA has not yet entered into force, but will do so when Mongolia brings certain laws into compliance with the terms of the TA. USTR and the GOM are working on this process.

9. Efficient Capital Markets and Portfolio Investment

Mongolia is developing the experience and expertise needed to sustain portfolio investments and active capital markets. In 2013 parliament passed the Revised Securities Market Law (RSML), which most investors believe creates a sufficient regulatory apparatus for these activities. The government of Mongolia (GOM) imposes few restrictions on the flow of capital in any of its markets. Multilateral institutions, particularly the International Monetary Fund (IMF), have typically found the regime too loose, especially in the crucial banking sector.

Money and Banking System, Hostile Takeovers

Although the government has clear rules about capital reserve requirements, loan practices, and banking management practices, the Bank of Mongolia (BOM), Mongolia's central bank, has historically resisted restraining credit flows and interfering with operations at Mongolia's commercial banks, even when the need to intervene has been apparent. In late 2014, the BOM began to pull back on a series of programs—a primarily a price stabilization program and a mortgage program—that had pumped trillions of Tugriks (MNT) into the economy leading to excessive liquidity, which the World Bank and the IMF say have contributed to the 42% depreciation of the MNT versus the U.S. dollar over the last two years. Inflation has lessened somewhat from a high of 13% in 2014 to 9.8% in January of 2015.

Weakness in Mongolia's banking sector concerns all players, including the International Monetary Fund (IMF: http://www.imf.org). The system has been through massive changes since the socialist era, during which the banking system was divided into several different units. This early system failed through mismanagement and commercial naiveté in the mid-90s, but over the last decade has become more sophisticated and somewhat better managed. As of January 2015, Mongolia's 14 banks (13 commercial banks and one state-owned bank) had combined assets of about US $10.7 billion. For more details on the banking sector, go to the Bank of Mongolia at http://www.mongolbank.mn/eng/default.aspx.

Mongolia has two large, generally well-regarded banks owned by both Mongolian and foreign interests. These two banks—Trade and Development Bank and Khan Bank—collectively hold approximately half of all banking assets. They apparently follow international standards for prudent capital reserve requirements, have conservative lending policies, up-to-date banking technology, seem generally well-managed, and are open to foreigners opening bank accounts under the same terms as Mongolian nationals. If a storm descends again on Mongolia's banking sector, these banks appear able to weather it.

From 1999 through late 2008, BOM consistently refused to close any commercial bank for insolvency or malpractice. In late 2008, Mongol Bank took Mongolia's fourth largest bank into receivership. Most deposits were guaranteed and their depositors paid out at a cost of around US$150 million -- not an inconsequential sum for an economy then hovering at a US$5 billion per annum GDP. In 2009, Mongolia's fifth largest bank went into receivership, and in 2010 two other mid-sized banks were merged; and in 2013, the BOM shut down Savings Bank for insolvency, merging it with the state-owned State Bank.

While the BOM and Mongolia's financial system have endured these chronic insolvencies, it is

notable that each failed bank had shown clear signs of distress before the BOM moved to safeguard depositors and the banking system. As with many issues in Mongolia, the problem is not lack of laws or procedures for dealing with troubled banks, which are sufficient to regulate the sector; but rather, some lack of capacity and an apparent reluctance on the part of BOM banking overseers to more aggressively enforce regulations related to prudential capital reserve requirements, bank management and corporate governance, and non-performing loans.

10. Competition from State-Owned Enterprises

Mongolia has State-owned Enterprises (SOEs) in energy production, mining, and transport. Investors have been allowed to conduct activities in these sectors, although in some cases an opaque regulatory framework limits both competition and investor penetration. Indeed, both foreign and domestic private investors believe that the current regime favors Mongolian SOEs over private enterprises. However, in early 2014 President of Mongolia Ts. Elbegdorj articulated a policy to privatize SOE's as part of his "Smart Government" initiative. Throughout 2014 and into 2015, both parliament and two successive governments took up the president's call, but neither has yet developed a legislative and administrative framework for privatization of SOEs.

Mongolia passed and implemented a competition law applying to foreign, domestic, and state-owned entities active in Mongolia. As a practical matter, competition between state-owned and private businesses had been declining for the simple reason that many parastatals had been privatized. Exceptions included the state-owned power and telecom industries, a state-owned airline, the state-owned rail system (half-owned by Russia), several coal mines, a fluorspar mine and a large copper mining and concentration facility (also half-owned by Russia). Currently, firms from Mongolia, China, Japan, Europe, Canada, and the U.S. have sought opportunities for renewable and traditional power generation in Mongolia. However, few want to invest in the power generation field until the regulatory and statutory framework for private power generation firms up and tariffs reflect commercial best practices and true cost recovery.

Regarding its railways, Mongolia has no plans to privatize its existing railroad jointly held with the government of Russia, but current law does allow private firms to build, operate, and transfer new railroads to the state. Under this law several private mining and foreign state-owned companies have proposed rail links, and obtained licenses to construct these new lines from their respective coal mines to the Chinese border or to the currently operating spur of the Trans-Siberian Railroad. At the moment, the Mongolia's rail policy requires that railroads linking key coal deposits in the South Gobi desert region must first link those deposits to Russia's Pacific ports before linking with Chinese markets. Further, these projects may use the international gauge (used in China and the U.S.) only after the links with Russia are completed, using Russian gauge. The GOM argues that this approach will keep Mongolia from being dependent on one market for its mining products, namely China. As construction on the Russian lines has stalled, there has been some progress on the China lines, with the road bed in the process of being laid. As of April 2015, issues around rail development for the South Gobi mines continued to be discussed in parliament.

Government Re-enters the Mining Business

Although the trend had been for the GOM to extract itself from ownership of firms and other

commercial assets, the 2006 Minerals Law of Mongolia (amended in 2014) and the 2009 Nuclear Energy Law keep the state in the mining business. Under both laws, the GOM grants itself the right to acquire equity stakes ranging from 34% up to 100% of certain deposits deemed strategic for the nation. Once acquired, these assets are vested with two state-owned holding companies respectively: Erdenes MGL, for non-uranium mining assets, and MonAtom, for uranium resources. State mandates require these companies to use proceeds from their activities to benefit the Mongolian people.

The role of the state as an equity owner, in terms of management of revenues and operation of mines, remains unclear at this point. Investors question the GOM's capacity to deal with conflicts of interest arising from its position as both regulator and owner-operator. Specifically, they worry that the GOM's desire to maximize local procurement, employment, and revenues may comprise the long-term commercial viability of mining projects. Investors also question the GOM's capacity to execute its fiduciary responsibilities as both owner and operator of mines. For example, through the Erdenes Tavan Tolgoi mining operation (ETT), the GOM received a prepayment of US $250 million for coal from a Chinese state-owned entity. Rather than allowing ETT to retain these funds to cover substantial startup costs, the GOM claimed the balance of the payment, US$200 million, for its Human Development Fund, which has redistributed primarily mining revenues to the Mongolian public in the form of monthly cash payments in 2012. ETT's debt to the Chinese SOE remains unresolved, and ETT finds itself owing public and private entities in excess of US $700 million, with very little to show for the debts incurred, according to investors familiar with ETT.

Investors worry that the GOM will divert future revenues gained from mining activities—for example capital raised through initial public offerings from strategic mines—for unrelated expenses. Going forward, the GOM will likely have to provide binding assurances that it can responsibly steward company interests rather than seeing state-owned companies as transfer mechanisms for payments to the Mongolian public. Observers are also concerned that the GOM may waive legal and regulatory requirements for state-owned mining companies that it imposes on all others. These concerns seem borne out by the GOM's treatment of state-owned ETT. Generally, private mining firms take at least two years to submit and receive approval for relevant environmental and operating permits for coal mines in Mongolia. However, there is no indication that from EET's inception in 2011 to the present that the GOM has required ETT's two operating mines to follow statutory or regulatory requirements imposed on other operations. A review of timelines suggests that the normally lengthy and costly approval processes cannot have been followed. This preferential treatment for this marquee SOE creates the appearance that the GOM has one standard for its SOEs and another for foreign-invested and private domestic invested companies; and also the appearance that SOEs receive substantial cost advantages via a more lenient interpretation or outright waiver of the legal requirements.

OECD Guidelines on Corporate Governance of SOEs

The State Property Committee (SPC), under the office of the Prime Minister, controls most Mongolian SOEs (excluding the Mongolian Stock Exchange, the Oyu Tolgoi and Tavan Tolgoi mines, certain mining properties, uranium properties and railroads). All SOEs, whether under the SPC or another entity generally report to the Prime Minister and Parliament. SOE's are technically required to submit to the same international best practices on disclosure, accounting,

and reporting as imposed on private companies. When SOEs seek international investment and financing, they tend to follow these rules. However, because international best practices are not institutionalized in, and are sometimes at odds with, Mongolian law, many SOEs tend to follow existing Mongolian rules by default. At the same time, foreign-invested firms follow the international rules, causing inconsistencies in corporate governance, management, disclosure, and accounting.

Mongolian SOEs do not adhere to OECD Corporate Governance Guidelines for SOEs: www.oecd.org/daf/ca/oecdguidelinesoncorporategovernanceofstate-ownedenterprises.htm.

Sovereign Wealth Funds

In 2008, Parliament established the Human Development Fund (HDF), ostensibly Mongolia's first sovereign wealth fund; however, it does not currently function as a sovereign wealth fund. The stated purpose of the law was to fulfill campaign promises to provide every citizen with cash payments in excess of U.S. $1,000 so that the public could benefit from Mongolia's mineral wealth. The HDF is to be funded from the profits, taxes, and royalties generated by the mining industry as a whole, including large, medium and small scale projects. The HDF basically serves as an instrument to distribute mining revenues to the citizens of Mongolia in the form of social benefits: Payments for pension and health insurance premiums; mortgage support and other loan guarantees; and payments for health and education services. The GOM has no plans to use the HDF as a conduit for Mongolian investments abroad or for FDI into Mongolia. In that sense, we find no conflict between the HDF and private sector investment. In 2014, Parliament discussed and Ministry of Finance officials publicly stated that they are drafting a new law to create a sovereign wealth fund. As of April 2015, no such draft law had appeared on Parliament's spring 2015 legislative agenda.

In 2011, Parliament created the Development Bank of Mongolia (DBM) for the explicit purpose of financing major infrastructure projects and support for export-oriented industries. Early plans were for the Development Bank to invest in cashmere processing, railways, power, and petroleum processing. The DBM's first tranche of sovereign debt was near U.S. $ 600 million, and has been followed up by an additional U.S. 500 million of borrowings. DBM investment practices have had no apparent impact on foreign direct investments in Mongolia.

Mongolia passed its Fiscal Stability Law (FSL) in 2010 (amended in 2015) as part of its Stand-By Arrangement with the International Monetary Fund that ended on September 30, 2010. In addition to setting a statutory limit to on-budget debt the state may take on, the FSL establishes a stabilization fund that sets aside certain mining revenues in excess of pre-set structural revenue estimates. Savings may then be used during a downturn to finance the budget. Under the FSL, a portion of the savings generated by the Fiscal Stability Fund can be used to finance domestic and foreign investments. For example, the government is allowed to use this money to purchase long term securities offered by the DBM to fund its activities. How the GOM and parliament will divide mining revenues between the HDF and the FSL remains to be determined, as Mongolia has yet to experience a surplus of these revenues.

11. Corporate Social Responsibility

It is early days for corporate social responsibility (CSR) in Mongolia. Most Western companies make good faith efforts to work with local communities. These efforts usually take the form of specific projects aimed at providing missing infrastructure—wells, power supplies, clinics or schools—or support for education such as books and scholarships. The larger Western firms tend to follow accepted international CSR practices and underwrite a full range of CSR activities across Mongolia; however, the smaller ones, lacking sufficient resources, often limit their CSR actions to the locales in which they work. Only the largest Mongolian firms regularly undertake CSR actions, with small- to medium –sized enterprises generally (but not always) hindered by limited resources from underwriting CSR actions. Generally, firms that pursue CSR are perceived favorably, at least within the communities in which they act. Nationally, responses range from praise from politicians to cynical condemnation by certain civil society groups of CSR actions as nothing more than an attempt to "buy" public approval. (For CSR in Mongolia refer to USAID sponsored Business Plus Initiative's web site: http://www.bpi.mn/. For information on the U.S. government approach to CSR-related issues see U.S. Government Approach on Business and Human Rights: http://www.humanrights.gov/2013/05/01/u-s-government-approach-on-business-and-human-rights/).

Mongolia has no broad statutory requirement for CSR actions covering all companies active in Mongolia. (Note: CSR is not statutorily required in the United States.) However, the 2014 Amendments to the 2006 Minerals Law require minerals exploration and mining companies to develop local development plans with the soum (county) in which they operate. Ministry of Mining officials explain that the GOM will codify and standardize how companies should work with soums on local development issues. To our knowledge these mining CSR standards remain un-promulgated.

OECD Guidelines for Multinational Enterprises

Generally, the GOM uses the bully-pulpit to exhort companies to adopt CSR practices, echoing admonitions of local NGOs and international institutions. However, these exhortations are inconsistent with the OECD principles set forth in the Guidelines for Multinational Enterprises or the United Nations' Guiding Principles on Business and Human Rights (OECD: http://mneguidelines.oecd.org/ncps/; UN Principles: http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf)

12. Political Violence

Mongolia is both peaceful and stable; political violence is rare. Mongolia has held eleven successful presidential and parliamentary elections in the past 19 years, though a brief but violent outbreak of civil unrest followed the disputed parliamentary elections on July 1, 2008. During that unrest, five people were killed and a political party's headquarters was burned. The violence was quickly contained and order restored, and no repeat of that level of civil unrest has occurred since. Indeed, Mongolia held peaceful presidential elections less than a year later in May 2009, in which the incumbent president was defeated and conceded at noon the next day; power was smoothly transitioned to the winner thereafter. Most recently, Mongolia held a politically robust, successful and peaceful series of elections (parliamentary in June 2012, local in November 2012,

and presidential in June 2013), that were generally marked by good voter turnouts, and peacefully conducted campaigns. The parliamentary elections resulted in a change of government, while the Presidential election returned the incumbent to office.

A more resource-nationalist tone in politics has become evident. Media and observer reports suggest a rising anti-foreigner sentiment among a few elements of the public, mostly based on the idea of wanting Mongolian resources developed in an environmentally sound, culturally sensitive way by Mongolians for the benefit of Mongolians. These concerns routinely inspire mostly peaceful protests–except for a September 2013 protest outside the Government Palace, during which rifles were fired into the air, and dummy explosive devices were placed in two nearby buildings. No one was harmed, the perpetrators were caught and convicted, and there has been no repeat of a similar event.

This nationalist sentiment has not led to any known incidents of anti-Americanism or politically motivated damage to American projects or installations since Mongolia established relations with the U.S in 1987. However, some commentators over the last three years have described a rising level of hostility to Chinese, Vietnamese, and South and North Korean nationals in Mongolia. This hostility has led to some instances of improper seizure of Chinese and Korean property, and in even more limited cases to acts of physical violence against the persons and property of Chinese—and to a lesser extent Korean and Vietnamese—nationals resident in Mongolia. There have also been rare and very isolated instances of physical violence directed at European and American foreigners in Mongolia.

13. Corruption

Since 2005, the USAID Mission to Mongolia, in collaboration with USAID/Washington and The Asia Foundation (TAF) has assessed corruption in Mongolia. (For USAID go to www.usaid.gov/mn.) These multiple reviews have found that opportunities for corruption have increased at both the “petty” or administrative and “grand” or elite levels. Both types of corruption should concern Mongolians and investors, but grand corruption should be considered the more serious threat because it solidifies linkages between economic and political power that could negatively affect or ultimately derail or delay democracy and development. Information from the USAID funded surveys are repeated in the U.S. Embassy’s annual Mongolian Human Rights Reports (MHHR) and the Investment Climate Statements. For the MHHR go to http://www.state.gov/j/drl/rls/hrrpt/humanrightsreport/index.htm#wrapper.

Current Anti-Corruption Law

In 2006, Parliament passed the Anti-Corruption Law (ACL), a significant milestone in Mongolia's efforts against corruption. In addition, the Criminal Code of Mongolia proscribes the acceptance of bribes by officials and provides for fines or imprisonment of up to five years for doing so. It also outlaws offering bribes to government officials. The ACL establishes the Independent Agency Against Corruption (IAAC) as the principal agency responsible for investigating corruption cases. The Organized Crime Department of the National Police Agency also investigates various types of corruption cases and often assists the IAAC in its investigations. (For a review of the IAAC’s activities from its inception through the present see The Asia Foundation Mongolia: http://asiafoundation.org/publications.)

In 2013, the MHRR reported that implementation of the ACL remains inconsistent, allowing corruption to continue at all levels of government. Factors contributing to corruption include conflicts of interest, lack of transparency, lack of access to information, a civil service system without adequate protection for government employees, and weak government control of key institutions. Of particular concern, members of parliament remain immune from prosecution during their tenure, which has prevented the prosecution of a number of allegations of corruption, and which can seriously restrict the scope of corruption investigations more broadly. Corruption-related prosecutions, however, increased during 2013 through 2014, and show no abating in 2015, having included a number of high-level officials from across the political spectrum, although questions of political motivation remain.

UN Anticorruption Convention, OECD Convention on Combatting Bribery

Mongolia is a State Party to the United Nations Convention Against Corruption (UNCAC), but not the Convention on Combatting Bribery of Foreign Public Officials in International Business Transactions (the Anti-Bribery Convention). (UNCAC: www.unodc.org/unodc/en/treaties/CAC/signatories.html; Anti-Bribery Convention: www.oecd.org/daf/anti-bribery/countryreportsontheimplementationoftheoecdanti-briberyconvention.htm.)

Resources to Report Corruption

Contact at Independent Agency Against Corruption (IAAC)
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Contact at Transparency International Mongolia
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14. Bilateral Investment Agreements

Bilateral Taxation Treaties

For a list of Bilateral Taxation Treaties Mongolia has signed with other nations go to UNCTD: http://investmentpolicyhub.unctad.org/IIA/CountryBits/139#iiaInnerMenu. In February 2015, Mongolia and Japan signed an Economic Partnership Agreement (EPA). The Parliament of Mongolia has since ratified the EPA, but Japan's legislature has yet to approve it. For more details on the EPA, go to http://www.mofa.go.jp/policy/economy/fta/mongolia.html. Although Mongolia and the United States have no bilateral tax or free-trade agreements, the two have signed and ratified a Bilateral Investment Treaty. For the BIT: http://2001-2009.state.gov/documents/organization/43579.pdf.

15. OPIC and Other Investment Insurance Programs

The U.S. government's Overseas Private Investment Corporation (OPIC: www.opic.gov) offers loans and political risk insurance to American investors involved in most sectors of the Mongolian economy. In addition, there is an Investment Incentive Agreement in force between the United States and Mongolia that requires the GOM to extend national treatment to OPIC financed projects in Mongolia. For example, under this agreement mining licenses of firms receiving an OPIC loan may be pledged as collateral to OPIC, a right not normally bestowed on foreign financial entities. Find an interactive map showing where OPIC has agreements at http://www.opic.gov/opic-action/interactive-map-overview. The U.S. Export-Import Bank (EXIM: www.exim.gov) offers programs in Mongolia for short-, medium-, and long-term transactions in the public sector and for short- and medium-term transactions in the private sector. Mongolia is a member of the Multilateral Investment Guarantee Agency (MIGA: www.miga.org).

16. Labor

The Mongolian labor pool is generally educated, young, and adaptable, but shortages exist in most professional categories requiring advanced degrees or vocational training. These shortages include all types of engineers and professional trades in the construction field. (For more on labor needs see: http://www.mca.mn/document/LMSReportMNG.pdf.) Unskilled labor is sufficiently available. Foreign-invested companies deal with these shortages by providing in-country training to their staffs, raising salaries to retain employees, or hiring expatriate workers to provide skills and expertise unavailable in Mongolia.

Mongolian labor laws are not particularly restrictive. Investors can locate and hire workers without using hiring agencies—as long as hiring practices are consistent with the Mongolian Labor Law. However, Mongolian law requires companies to employ Mongolian workers in all labor categories whenever a Mongolian can perform the task as well as a foreigner. This law generally applies to unskilled labor categories and not areas where a high degree of technical expertise is required but does not exist in Mongolia. However, if an employer seeks to hire a non-Mongolian laborer and cannot obtain a waiver from the Ministry of Labor for that employee, the employer can pay a monthly waiver fee. Depending on a project's importance, the Ministry of Labor can exempt employers from 50% of the waiver fees per worker. However, employers

report difficulty in obtaining waivers, in part because of public concerns that foreign and domestic companies refuse to hire Mongolians at an appropriate level.

The Labor Law entitles workers to form or join independent unions and professional organizations of their choosing without previous authorization or excessive requirements and protects rights to strike and to collective bargain. However, some legal provisions restrict these rights for foreign workers, certain public servants, and workers without formal employment contracts, although all groups have the right to organize. The law protects the right of workers to participate in trade union activities without discrimination, and the government has protected this right in general. The law provides for reinstatement of workers fired for union activity, but the Confederation of Mongolian Trade Unions (CMTU) stated that this provision is not always enforced. According to the CMTU, some employees faced obstacles to forming or joining unions, and some employers took steps to weaken existing unions. For example, some companies would use the portion of employees' salaries deducted for union dues for other purposes, not forwarding the monies to the unions. Some employers prohibited workers from participating in union activities during working hours, even though by law workers have the right to do so. There have also been some violations of collective bargaining rights, as some employers refused to conclude collective bargaining agreements.

The law on collective bargaining regulates relations among employers, employees, trade unions, and the government. Wages and other conditions of employment are set between employers (whether public or private) and employees, with trade union input in some cases. Laws protecting the right to collective bargaining and freedom of association generally were enforced. The tripartite Labor Dispute Settlement Committee resolved the majority of disputes between workers and management. Cases that could not be resolved at the Labor Dispute Settlement Committee are referred to the courts. (For more on Mongolian labor laws as they relate to union activity refer to Mongolia Country Reports on Human Rights Practices for 2013 at http://www.state.gov/j/drl/rls/hrrpt/humanrightsreport/index.htm#wrapper.)

For a list of International Labor Organization (ILO) conventions ratified by Mongolia go to http://www.ilo.org/dyn/normlex/en/f?p=1000:11200:0::NO:11200:P11200_COUNTRY_ID:103142.

17. Foreign Trade Zones/Free Ports/Trade Facilitation

The Mongolian government launched its free trade zone (FTZ) program in 2004. Two FTZ areas are located along the Mongolia spur of the trans-Siberian highway: one in the north at the Russia-Mongolia border town of Altanbulag; the other in the south at the Chinese-Mongolia border at the town of Zamyn-Uud. Both FTZs are relatively inactive, with development pending at either site. A third FTZ is located at the port of entry of Tsagaan Nuur in the far western province of Bayan Olgii. Mongolian officials also suggest that the New Ulaanbaatar International Airport (NUBIA), expected to commence operations in 2017, may host an FTZ. In April 2004, the USAID sponsored Economic Policy Reform and Competitiveness Project expressed the following concerns about Mongolia's FTZ Program, which remain valid in 2015. First, benchmarking of Mongolia's FTZ Program against current successful international practices shows deficiencies in the legal and regulatory framework as well as in the process being followed to establish FTZs in the country. Second, FTZ's lack of implementing

regulations required to implement key international best practices. Attempts to update the relevant laws and regulations remain ongoing. Third, a process of due diligence, including a cost-benefit analysis, has never been completed for the FTZs. Fourth, sufficient funding has never been mobilized for on-site infrastructure requirements for the three FTZ sites. Finally, deviations from international best practices in the process of implementing FTZs repeats mistakes made in other countries and may lead to "hidden costs" or the provision of subsidies that the government of Mongolia did not foresee or which will have been granted at the expense of higher priorities.

18. Foreign Direct Investment and Foreign Portfolio Investment Statistics

Table 2: Key Macroeconomic Data, U.S. FDI in Host Country/Economy

	Host Country Statistical source*		**USG or international statistical source**		**USG or International Source of Data: BEA; IMF; Eurostat; UNCTAD, Other**
Economic Data	**Year**	**Amount**	**Year**	**Amount**	
Host Country Gross Domestic Product (GDP) ($M USD)	2013	11,500	2014	12,000	www.worldbank.org/en/country

Foreign Direct Investment	**Host Country Statistical source***		**USG or international statistical source**		**USG or international Source of data: BEA; IMF; Eurostat; UNCTAD, Other**
U.S. FDI in partner country ($M USD, stock positions)	2012	62.6	N/A	N/A	BEA data available 3/19/14 at http://bea.gov/international/direct_investment_multinational_companies_comprehensive_data.htm
Host country's FDI in the United States ($M USD, stock positions)	N/A	N/A	N/A	N/A	BEA data available 3/19/14 at http://bea.gov/international/direct_investment_multinational_companies_comprehensive_data.htm
Total inbound stock of FDI as % host GDP	N/A	N/A	N/A	N/A	N/A

Mongolia Host Country Data: National Statistical Office, Mongolian Statistical Year Book, 2013: www.nso.mn

Table 3: Sources and Destination of FDI

Generally, Mongolia's data on in-bound foreign direct investment tallies with Mongolian domestic statistics available from the Invest Mongolia Agency (IMA). However, Mongolia does not track where the beneficial ownership of a given investment actually terminates, but only where the company claims to be domiciled. We are aware of numerous cases where foreign entities active in Mongolia do not incorporate in their countries of origin but in third countries, largely for tax mitigation purposes. Consequently, although Mongolia's data and the IMF's respectively suggests that much of Mongolia's investment originates from such places as the Netherlands or Singapore, much of the investment comes from other jurisdictions.

Direct Investment from/in Counterpart Economy Data

From Top Five Sources/To Top Five Destinations *(US Dollars, Millions)*

Inward Direct Investment			**Outward Direct Investment**		
Total Inward	13,458	100%	Total Outward	N/A	100%
Netherlands	7,637	57%	N/A	N/A	N/A
Singapore	1424	11%	N/A	N/A	N/A
United Kingdom	906	7%	N/A	N/A	N/A
PRC China	657	5%	N/A	N/A	N/A
Hong Kong SAR	544	4%	N/A	N/A	N/A

"0" reflects amounts rounded to +/- USD 500,000.

Source: IMF Coordinated Direct Investment Survey

Table 4: Sources of Portfolio Investment

Mongolia does not track portfolio investment, so there is no basis for comparison with the IMF's Coordinated Portfolio Investment Survey data.

Portfolio Investment Assets

Top Five Partners (Millions, US Dollars)

Total			**Equity Securities**			**Total Debt Securities**		
All Countries	387	100%	All Countries	379	100%	All Countries	9	100%
Hong Kong SAR	253	65%	Hong Kong SAR	253	69%	Honduras	3	39%
Australia	34	9%	Australia	33	9%	Singapore	2	28%
Honduras	34	9%	Honduras	31	8%	United States	2	21%
United States	26	7%	United States	25	6%	Australia	1	7%
Singapore	15	4%	Singapore	11	3%	Russian Federation	0	2%

Source: IMF Coordinated Portfolio Investment Survey

19. Contact for More Information

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