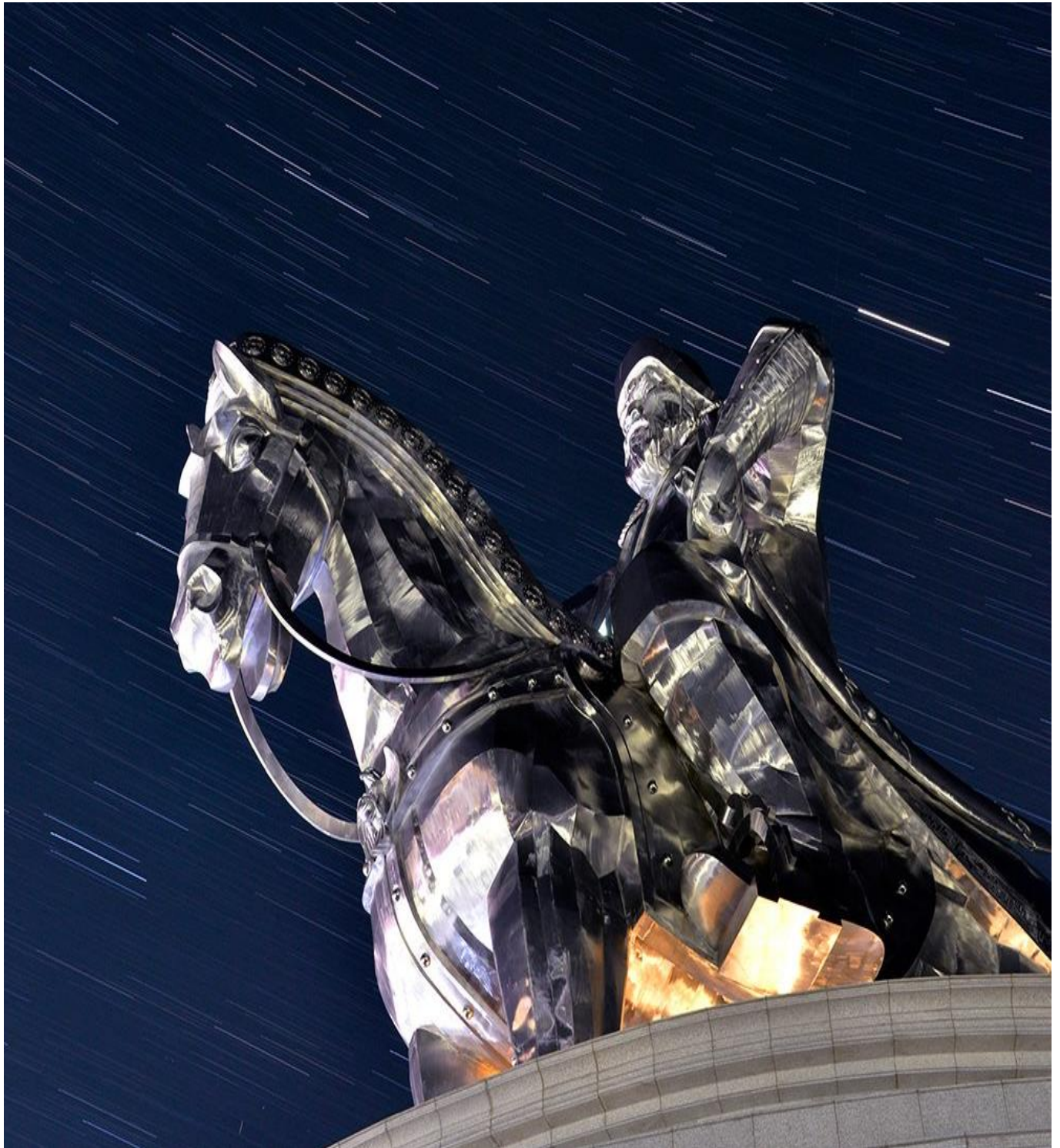
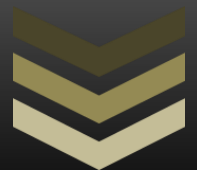


DECEMBER 2018

updated JANUARY 2019



**PROPOSED AMENDMENTS TO  
THE MINERALS LAW OF  
MONGOLIA**



Dear Client,

We have updated the below advisory circulated to you in December 2018. The updates (additions) are included into this advisory as Part Four and highlighted in yellow (below).

## AMENDMENTS TO THE MINERALS LAW OF MONGOLIA ARE BEING DISCUSSED IN THE PARLIAMENT OF MONGOLIA

The current Minerals Law of Mongolia was first adopted in 2006 (and amended several times since then) (the “**Minerals Law**”). Earlier this year, a draft law proposing certain amendments to the Minerals Law, prepared by the Government of Mongolia (the “**Draft Law**”), is being discussed in the State Great Khural of Mongolia (the “**Parliament**”). On 4 December 2018, the Economic Standing Committee of the Parliament discussed the Draft Law and forwarded it to a full session of the Parliament for further discussions.

### One. Rationale for the Draft Law

If the Draft Law is adopted as currently drafted, according to the Government of Mongolia, the following three key changes would be made to the Minerals Law:

1. Prior to 2014, the following royalties had been payable on gold sold or used:
  - flat-rate royalty at the rate of 5 percent of the sales value; and
  - surtax royalty at the rate ranging between zero and 5 percent of the sales value depending on market price of gold.

Efforts to evade the above royalties had produced negative consequences, such as wide-spread illegal smuggling of gold. Subsequently, in 2014 the Parliament has reduced the rate of the above royalties to 2.5 percent. Following the reduction, the amount of gold sold domestically to the Bank of Mongolia (Central Bank) has risen from 12.7 tons in 2014 to 20 tons in 2017. This has in turn contributed to the increase in foreign-exchange reserves of the Bank of Mongolia.

However, effectiveness of Article 47.3.3 of the Minerals Law, which has set the royalty at 2.5 percent in 2014, is due to expire on 1 January 2019. Upon expiry of effectiveness of Article 47.3.3 of the Minerals Law on 1 Jan 2019, the rate of royalties for gold would increase back to the pre-2014 rates (set above). Thus, according to the Draft Law, the Government of Mongolia is proposing to extend effectiveness of Article 47.3.3 (i.e., the operation of 2.5 percent royalty) for another 5 years, i.e., until January 1, 2024.

2. According to the current Minerals Law, only legal entities who hold mining licenses in Mongolia are subject to royalties, calculated from sales value of minerals sold, shipped for sale or used from a mine site. Such limited tax base of royalties leaves out other parties who have been active in gold mining in Mongolia – namely, artisanal or micro miners, as well as mineral processing plants. None of these parties hold, or are required to hold, mining licenses. According to the Draft Law, the following parties would become subject to paying royalties – (i) a legal entity, which sells, or ships to sell, or use minerals, and (ii) an individual or a legal entity, who sells gold to the Bank of Mongolia, or to a commercial bank (authorized by the Bank of Mongolia to purchase gold). According to the Government of Mongolia, the Draft Law would lead to an increase in the royalty revenues for the state budget by widening the tax base.

3. Currently, there is no established system for reporting of royalties, withheld and transferred by the Bank of Mongolia and/or commercial banks to the state budget of Mongolia. According to the Draft Law, the Bank of Mongolia, or commercial banks (authorized by the Bank of Mongolia to purchase gold), would have an obligation to submit tax reports on royalties withheld and transferred by them to the state budget.

## **Two. Expected outcomes of the Amendments to the Minerals Law**

If the Draft Law is enacted as currently drafted, according to the Government of Mongolia, it would lead to the following outcomes:

- a) create statutory grounds for imposing tax obligations on individuals and legal entities, which currently do not hold mining licenses, to pay royalties if they gold to the Bank of Mongolia, or to a commercial bank (authorized by the Bank of Mongolia);
- b) establish a reporting system on royalties withheld and transferred by the Bank of Mongolia, or commercial banks (authorized by the Bank of Mongolia) to the state budget;
- c) increase volume of gold, sold to the Bank of Mongolia, and, by extension, of foreign-exchange reserves of the Bank of Mongolia which would further support stability of Mongolian tugrik;
- d) lead to better collection of royalties to the state budget of Mongolia; and
- e) widen the Mongolian tax base.

## **Three. Highlights**

If the Draft Law is adopted as is, in addition to the above-mentioned outcomes, the following persons, who do not currently hold mining licenses, would be subject to royalties:

- Any legal entity, which sells minerals (i.e., without mining license);



- Any legal entity, which ships minerals for sale (i.e., without mining license);
- Any individual or legal entity, which sells gold to the Bank of Mongolia, or a commercial bank (authorized by the Bank of Mongolia).<sup>1</sup>

As a result, according to the Government of Mongolia, the Mongolian tax base will be broadened as new parties will have obligations to pay royalties, even if they do not have mining licenses.

We expect that following the adoption of the Draft Law, Mongolian tax or other relevant governmental authorities will adopt further detailed regulations related to registration of new royalty payers, receipt of their reports and royalty payments to the state budget of Mongolia.

#### Four. Impasse in the Parliament and resulting automatic reinstatement of pre-2014 rates

Due to internal political standoff within the governing Mongolian People's Party (which controls 64 out of total 76 seats of the Parliament), no session of the Parliament has occurred for the last four weeks. In particular, the majority members of the Parliament (over 40 members) have boycotted sessions of the Parliament until the resignation of the speaker of the Parliament citing ethical misconduct grounds. The speaker has in turn rejected the allegations and refused to step down. As a result, all matters being discussed at the Parliament, including the Draft Law on Amendments to the Minerals Law of Mongolia, have stalled.

Meanwhile, the effectiveness of Article 47.3.3 of the Minerals Law, which set the royalty for gold at 2.5 percent in 2014 (as discussed above), has expired on 1 January 2019. As a result, the rate of royalties for gold has automatically increased back to the pre-2014 rates as follows:

- flat-rate royalty at the rate of 5 percent of the sales value; and
- surtax royalty at the rate ranging between zero and 5 percent of the sales value depending on market price of gold.

It means that unless the Draft Law is enacted, gold miners must pay the royalty at the above pre-2014 rates.

It is our understanding that the Government of Mongolia, which has originally submitted the Draft Law to the legislature in 2018, is still intent on the Draft Law being adopted by the legislature as soon as possible. However, at the moment, it is unclear to us when the Parliament will resume functioning and whether the Parliament will

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<sup>1</sup> In an unlikely scenario, when a party sells gold to any buyer other than the Bank of Mongolia, or commercial bank authorized by the Bank of Mongolia, the standard flat-rate royalty (5%) and surtax royalty (0-5%) would be applied.

approve the Draft Law as currently drafted. We note that there are members of the Parliament, who have been vocal in supporting reinstatement of the royalty back to the pre-2014 rates.

KhanLex Partners will continue monitoring the situation and updating its clients on further developments with the Draft Law.

If you wish to receive further information about the Minerals Law, please contact Mr. Batjargal Gombosuren (Partner), tel: (+976) 9900-1070 (m), (+976) 7747-1122 (o), e-mail: [batjargal@khanlex.mn](mailto:batjargal@khanlex.mn).

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