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DeFacto **ARTICLE**

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## Gold FEVER

**ARTICLE**

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## THE INVESTMENT CLIMATE

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# Gold FEVER

*Photo credit: Undesnii Shuudan newspaper*

Gold is one of very few commodities that does not lose its value at any given time or circumstances. Mongolia's first president P.Ochirbat viewed that gold was the only way to overcome the 1990s economic crisis and initiated the Gold programme. Subsequently, the Gold-2000 programme was implemented from 2000, and the Gold-2 programme from 2017. As of 2017, Mongolia had mined 200 tonnes of gold (worth 2.8 billion USD).

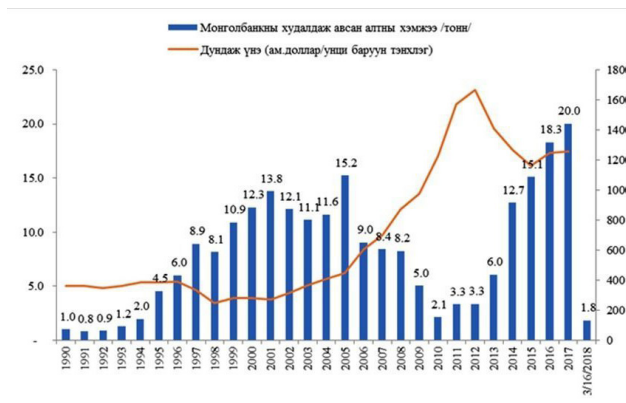
“ *Mongolia's economy was injected with these programmes focused on gold every ten years.* ”

Even though the gold injections revived the economy, we now need to come together as a society and reflect on what consequences have been brought on the environment, economy, and society. »

## ► GOLD AND TAXES

Seventy-five per cent of Mongolia's export revenue comes from coal, copper, and gold. Mongolbank bought 15 tonnes of gold in 2005, but only two tonnes in 2010. But the number grew back gradually and reached 20 tonnes for the first time in 2017. This drastic drop and the subsequent rise were created by tax policies from the government.

*[Amount of gold purchased by Mongolbank]  
[Average price, USD per ounce]*



Gold is mined by companies and individuals. When the windfall profits tax was introduced at 68 per cent in 2006, Mongolia's gold industry went underground. In addition, if business entities recorded a revenue of over 3 billion MNT, they had to pay a 25-per-cent tax. It forced the gold miners to sell their gold to Mongolbank via individuals. This was also not helped by a 5-per-cent royalty. It also increased the illegal trade of gold sold over the border. All of these factors resulted in a decrease of Mongolia's gold reserves and weakening tugrug.

In 2010, the government changed its policy, cancelling the windfall profit tax, reducing the royalty rate for gold to 2.5 per cent, and nullifying the abovementioned business entity tax for five years. This gradually prompted people to increasingly trade gold with Mongolbank, which culminated in 2017 when Mongolbank set a new record, having purchased 20 tonnes of gold.

“ Individual gold miners ('ninjas') currently comprise a significant portion of Mongolia's labor market. Today we have 8,000 registered ninjas and nearly 30,000 unregistered ones moving around the country to wherever they have heard gold is. ”

There is a gold fever going on, where ninjas are fiercely competing with each other to find gold, without time to eat or go home. The traces of Mongolia's gold fever are evident in the pits and holes in the ground and the remains of animals that fell and died there, found in dozens of soums including Zaamar, Sumber, Mandal, Biger, and Urgamal.

The ninjas try their best to spend the night selling the rice-like gold they found during the day, so that they can start looking for bigger finds the following day.

“ The real owners of these ninjas are the 'secret lords' who pay them with cash in exchange for the gold. The secret lords then collect the gold, mould them together, and sell to Mongolbank at international rates using an individual's name and paying a tax of only 2.5 per cent. ”

The local government does not even bother talking about protection of environment with ninjas. It is because the local government is usually the one who starts and encourages the gold fever in the first place.

The government is currently pursuing a policy to retain the gold in-country by purchasing them without checking where and how it was mined and almost without asking for any tax.

“ Our government has become unable to enforce rules and regulations, so they chose to cut the taxes in order to not lose the gold. This is what is special about Mongolia's gold fever. ”►

## ► LEGAL ECONOMY AND UNDERGROUND ECONOMY

If the tax on gold is high, gold miners choose not to sell to Mongolbank, but to smuggle gold abroad for cash and goods. This increases the growth of person-to-person trade. When gold does not go through the bank, the circulation of cash slows down while the underground economy expands. Also, individual traders do not pay taxes, which strengthens the underground economy.

In contrast, businesses operating in the legal economy create jobs and pay an amount equal to one third of salaries to the government in the form of medical insurance and personal income tax. The individual traders feed on it because they are covered by medical insurance despite not paying taxes. As a result, the amount covered by our medical care is never enough.

*“The secret lords of gold mining have been growing so big that they have now become the hidden financiers of political parties.”*

Given that they have already paid up, these secret lords have started to decide whether the central or local government should give mining licences and permits. It also looks like they are in control of which laws to pass and which ones to be postponed.

Under a government decree, the regulations pertaining to micro mining were passed, which allowed local governors (at soum and district levels) to give ninjas permits to conduct mining activities. As soon as this decree was issued, some governors started receiving bribes and even began their own gold mining.

The members of local citizens' representatives khural are now behaving like they govern their own country. For example, an Umnugovi governor said

that any mineral resources found in the territory of Umnugovi aimag shall foremost belong to the people of Umnugovi. The citizens' representatives' khural of Umnugovi aimag once decided on their own to ban the use of water for mining activities in the territory of the aimag.

*“We are also seeing groups that instigate ninjas under the name of the people.”*

In Khuvsgul, Sukhbaatar, and Bayankhongor aimags, ninjas attacked mining companies to do their own gold mining. As soon as gold reserves are estimated, ninjas are the first people who come to the site. Steppe Gold Company had not even started their operations when ninjas attacked their mine in groups and chased away their employees. As a result, the company's shares saw a drastic fall on the Toronto Stock Exchange.

Mining and Heavy Industry Minister D.Sumiyabazar made a vague statement and said “law enforcement, especially the police, is connected to the case” when explaining why the gold mining at Noyon Mountain had been disrupted. The police and law enforcement are serving the secret lords.

*“Today Mongolia's people and government are both experiencing a gold fever.”*

If we see the government start enforcing rules, the business environment improves, officials stop doing their own businesses under the name of the government, and the private sector sees free competition, then business will expand and create jobs that would prompt ninjas to go home.

2018.08.23 ■





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ARTICLE

# THE INVESTMENT CLIMATE

As we head into the first week of September, conference season is upon us, with a number of investor-related events taking place in the space of just 5 days, including traditional annual events such as Coal Mongolia, Discover Mongolia and the IWFCI Global Women's Trade Summit.

“All in all, a crazily busy week, but before the storm breaks it may be worthwhile looking at some key areas where investment has been active, where significant investment is required, and reflecting on the state of investor

*confidence in Mongolia as an investment destination.*”

Following the IMF bailout in 2017, the economy as a whole is performing well it seems largely off the back of improved or at least consistent commodity prices. Coal exports are certainly better with both Erdenes Tavan Tolgoi and Hong Kong listed MMC reporting improved results, and are an important driver for export revenues. Current projections show an expected GDP growth of between 6-7 per cent in 2018.

## BUOYANT ENERGY SECTOR

A significant amount of activity has been seen in the renewable energy sector which has continued to be very active over the past 18 months. A number of new projects have been developed, including the 55MW Sainshand Wind Park during the course of this year requiring over USD 100 million investment from partners ENGIE, Ferrostaal, EBRD, European Investment Bank and the Danish Climate Investment Fund. This project is expected to come online towards the end of 2018. This followed on from the commencement of operations in late 2017 at the 50 MW Tsetsii Wind Farm, supported by Clean Energy Asia, a joint venture between Newcom and Softbank Energy, with financing from EBRD and JICA.

The solar power sector has also been highly active, with a number of projects closing successfully or under development and construction. These included Sharp Corporation and Shoji Shigemitsu's 10MW solar plant in Darkhan, completed in 2016; a second solar power plant developed by Sharp and Shigemitsu of 15 MW in Zamyn-Uud; and a 30 MW solar plant at Sainshand

backed by a loan from the EBRD and FMO, the Dutch Development Bank. A number of other projects are currently under consideration, all of them sponsored or supported by private sector players.

One caveat to this is that the capacity for renewable energy in Mongolia may be drawing to a close. The electricity grid infrastructure is ageing and according to the World Bank, sections of the grid see up to 25% distribution losses, with infrastructure upgrades required in order to bring further renewable projects online. If Mongolia is to participate in a form of Asian Super Grid, a project that has been discussed for many years, these infrastructure upgrades will be vital.

A number of other areas in the energy sector are being actively explored, including long term projects to develop coal bed methane natural gas production, as a cleaner fuel. This may also have the benefit over time of reducing the serious levels of winter pollution that plague Ulaanbaatar for three months of the year. ►►

## ► NEED FOR URBAN INFRASTRUCTURE

As urbanisation inexorably impacts Ulaanbaatar city, there is a lot that can and needs to be done around urban infrastructure.

This ranges from water management projects, to developing a distribution hub for imports and exports.

Developing a logistics and warehouse centre to improve distribution systems for import and export of goods is an increasingly important area for development. Combined with the new Ulaanbaatar International Airport there is significant potential for synergies in this sector, which would help to resolve bottlenecks in product distribution and potentially lower prices to the end consumer.

As regards water management, another key issue

for Ulaanbaatar, in 2018 the Millennium Challenge Corporation approved a USD 350 million compact to move forward with a Water Supply Project, which would involve construction of new groundwater wells downstream from Ulaanbaatar, a state-of-the-art water purification plant, construction of a new freshwater recycling plant and pipelines to provide high-quality treated freshwater, and policy and technical assistance support. MCC estimates that these projects will increase the supply of water to Ulaanbaatar by more than 80 percent.

These are some of the highlights of mainly private sector development projects over the past year and looking to future economic growth. What about the public sector and government-driven projects?

## WHERE ARE THE MAJOR PROJECTS?

One area that has been disappointing since the 2016 election is in the sphere of so-called major projects. None of the major, largely energy and mining related, projects that have been on the radar over the past five years, such as CHP-5, Egiin Gol Hydropower Plant, TTPP, the development of TT itself and the railway network.

There is not a lot of time left for this government to develop projects of this nature which typically take several years to come online. That said, there are some encouraging signs with recent moves to seek a listing for ETT and cabinet decisions last month to move forward with the Gashuunsukhait border railway.

## INVESTOR CONCERNS

While two of the conferences next week will be heavily focused on the mining sector, this of course remains the locomotive of the economy, and it will be interesting to hear the views of investors on the current climate. There are undoubtedly many issues, from pressure on Oyu Tolgoi, which foreign investors treat as a barometer of the government's attitude to FDI, to ninja miners, visa problems, ongoing licence suspensions and difficulties in dealing with soum and aimag level local government in moving projects forward. An additional concern is the fact that elections in 2020 are not far away, and politicisation of existing projects will become an issue.

Mining remains a mixed bag, given the recent negative experiences of a number of foreign investors, however investors are always looking for opportunities to develop Mongolia's mineral resources and interest is likely to continue to grow as the commodities market has improved.

Policymakers need to recognise that Mongolia is always competing with other developing countries such as those in Latin America and elsewhere in Asia. This should be front of mind when creating a coherent longer-term strategy for the nation's development that does not focus on short-term wins.

“ *My own take on the FDI climate is that things are clearly improving in certain areas, such as banking and finance (including interest in cryptocurrency and derivatives transactions), renewable energy and broader long-term energy solutions.* ”

August 2018 ■



## GOVERNMENT RELAUNCHES THE NATIONAL COMMITTEE ON LAND RENOVATION

*In Mongolia since the 1990's, land has been allocated randomly, without any organized system. This has been a major cause of frustration and dispute amongst citizens and endangers many lives because of unauthorized use of land. The National Committee on Land Renovation was established in 2017. The first meeting of the Committee was held on Tuesday August 21st, 2018. The committee discussed short-term coordination of urgent tasks to systematize and unify the registration of land use and ownership.*

The National Committee of Land Renovation is a structured one under the Prime Minister competency. The idea of this coordination is very old in democratic Mongolia. Since 2000, Mongolia was able to have all the cadastral maps of all soums, aimags and Ulaanbaatar city. The only issue was that it needed to be approved as it was, but because it was under one ministry, all ministries took a pie from this. There was always an issue of where to mine and where not to mine, if it were a reserved area or not etc. In other words, there has always been a problem with coordination of decision related to land, which gets worse in the case of Ulaanbaatar city.

The PM luckily established this committee and they had this meeting, but it is questionable if these resolutions can solve the problem in the long run. Because we have seen many committees and laws that remain on paper and unimplemented. Countries that have these kinds of problems often times start with corruption, instability and maybe civil war because it is the base of prosperity of any country. The difference this committee is making is that all land-related agencies and ministries are now working under the PM.

*The most urgent action related to land has always been to have clear inventory of land, called registration. Second*

*is "who owns it?" and third is "who uses and possesses it?". These issues are not clearly met in public property regulations, including the land.*

The blurry borders between them make good soil for corruption, which is successfully used by Mongolian politicians. The best example is Ulaanbaatar city. Bogd Khan Mountain, south of the city, supposedly has been a protected area for 800 years now, but who is protecting from whom? The Ministry of Natural Environment is supposed to protect our land, but now we need to protect our land from this ministry. Different administrations of the ministry have been giving away the land under the table, which, the money in return goes to their political party.

That is why we need a solution to land problems. There should be a clear and integrated database so that corruption cannot take place. Hopefully this committee can solve corruption issues, but bear in mind that they will also have to combat their own parties and corrupt officials. It is especially hard with two dominating parties that are either together or fighting each other, so the efficiency is doubtful.

## PARLIAMENTARY BY-ELECTION DATE DECLARED INVALID BY THE CONSTITUTIONAL COURT

*13 political parties are approved to compete in the parliamentary by-election to newly represent around 22,000 citizens of Khentii aimag. The special election was announced in July of 2018 and scheduled on October 7th, 2018. However, on Wednesday last week, the Constitutional Court of Mongolia has declared the date invalid because according to law, public servants must be given 6 months' notice so they can resign and run for elections. The next possible date is likely to be in June or October of 2019. There are 3 soums from Khentii province that are in question, they would be left unrepresented if the election date remains postponed.*

It is unlikely that the by-election is going to take place on time because it is not in favor of the ruling party (65 seats out of 76). The former parliament member from this electorate has been accused of raping, making it harder for the ruling party, added to the risk of political balance as it is a mid-term election. This puts the ruling party in a hard position, so they will try to make sure that the by-election doesn't take place, starting with the constitution. There will also be another voice from the 13 political parties, making it less pleasing.

Even if the by-election takes place in June or October of 2019, it is only a year away from the next election, which is too short and the ruling party will most likely make this another reason not to have the election. The Constitutional Court often times works for the parliament rather than the people, which can be seen from many cases. The Constitutional Court itself is violating the law because its headquarter is in Zaisan, a protected land by the law. In the end, the parliament will decide whether to accept this date or not, which is most

likely going to be in favor of the ruling party and hence, no by-election.

We know that Ms. Munkhtsetseg wants to run for the election as of now, but we don't know which party she's from and it's unclear whether she is from Khentii aimag either.

*In the end, the decision-makers should think about whether it is just a matter of one public officer running for office, or 22 thousand people that are not being represented. However, it doesn't look like the Constitutional Court will take these 22 thousand people and Ms. Munkhtsetseg's interest into account, which creates a very clear image of our political landscape.*

Further measurements and alternative approach will

be discussed at the fall session of the parliament. If the by-election takes place, the People's Party will most likely not win, exacerbating the discussion on corruption, the 60 billion tugriks scandal. The by-election will also drive the already-distant party apart as well.

The General Election Committee has decided that the Civic Will Party cannot join the by-election because they didn't submit their financial report of the last election. But if all these 13 parties have submitted their reports, where are they? They are not using it for personal reasons, so it should be up on their website, in public. By doing this, they are also cooperating with Mongolian corrupt officials. Instead of having a General Election Committee, one idea is to have General Electorate Committee, where non-partisans take control instead of the two parties.

## MISCONDUCT OF FORMER MINISTER, Z. BAYANSELENCE

*Former Minister of Construction and Urban Development, Mrs. Bayanselenge was indicted with charges including misuse of power and \$400,000 in damages on Wednesday last week. In 2015, she approved herself to purchase 720 apartments from Beren Group for \$6 million from the state budget as part of her initiative called "Housing for rent." The initiative was aimed at reducing ger districts and renewing the urban plan in Ulaanbaatar. The former minister claims that her indictment was set up by political oppositions.*

Mrs. Bayanselenge comes from Mongolian People's Revolutionary Party, which is where the People's Party originated from. She was a minister during the coalition government and during her time, she allowed private companies to sell 720 residential apartments for renting without tender, which she says has no loss in it. Whether she was personally involved in this matter or bought apartment for her relatives is not clear.

The Court has decided that she is to pay 19 million tugriks, derived from minimum wage, which some people find to be inadequate. However, we should also think about if she would have received the same amount of penalty if she had been in one of the two dominating parties. Throughout political history, members from these two parties have only been arrested for a few months at the best and released due to medical conditions or any other reason, but never punished

as severely as members from other parties were. Even the court seems to work harder when it comes to people against political interests of these parties.

*It is unclear how the "big-named" bonds like Chinggis and Khubilai bond have put us into this big debt and we don't see reports on how the money was used either. Yet, the state is giving this much penalty to this woman because she doesn't belong to the two main parties.*

Mrs. Bayanselenge also claims that this was because she revealed a closed cabinet session regarding the 49% ownership of Erdenet company as she was a cabinet member when this purchase happened. She revealed the footage a day before the election, causing the Democratic Party to lose. Therefore, it could somehow be related to this incident.



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*This review has been edited here for space and clarity. You can watch the full 30-minute review on the Defacto website [\[HERE\]](#).*





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